Synlait

ANNUAL REPORT 2020

Certified B Corporation

Synlait's commitment to elevating people and planet to the same level as profit was recognised in June 2020 when it became part of the B Corp™ community.

B Corp™ is a community of leaders driving a global movement of people using business as a force for good. Certified B Corporations™ consider the impact of their decisions on their workers, customers, suppliers, community, and the environment.

This movement resonates strongly with Synlait's purpose of *Doing Milk Differently For A Healthier World.*

Learn more about what being a B Corp™ means for our people, our community, and our customers at: **synlait.com/bcorp**

ABOUT THIS REPORT

Welcome to our Annual Report.

This annual report reviews Synlait Milk Limited's (Synlait) and subsidiaries financial performance and business achievements for the year ended 31 July 2020.

It represents our first step towards adopting Integrated Reporting methodology. We have been guided by the principles of Integrated Reporting to demonstrate to you, our shareholders, how we create value.

Driven by our purpose of *Doing Milk Differently For A Healthier World* we are making genuine progress to diversify Synlait and progress our ambition, which we call: 2 + Zero. We are well placed to deliver sustainable growth for you, while balancing people, planet and profit in our decisions. We hope you find our progress encouraging.

We always look for ways to improve our reporting, please email any feedback to: **investors@synlait.com**

An online copy of this report and our previous annual, interim and sustainability reports are available at: **synlait.com/investors/**

REPORT ICONS

Did you know

Learn more

SUSTAINABILITY

For shareholders interested in Synlait's environmental and social impact, a standalone sustainability report will be released in November. This report will review Synlait's strategy and initiatives to deliver on our sustainability objectives and targets.

It is our intention to merge the sustainability report into the annual report over time.

Tankers line up to unload at the Synlait Dunsandel milk reception bay.

DIFFERENTIATED MILK SUPPLY

Our differentiated milk supply is what sets Synlait apart and enables us to manufacture specialty products with a higher value. Special milk programmes require farmers to add value for our customers behind the farm gate, such as a1 protein-free, Lead With Pride™ or grass fed milk. We recognise this value by paying premiums on top of our base milk price.

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Synlait Dunsandel

HIGHLIGHTS FROM THE YEAR

RESULTS AT A GLANCE

Synlait remains a solid and highly profitable business despite COVID-19.

EBITDA grew strongly demonstrating the strength of our infant and lactoferrin businesses.

NPAT reduced reflecting investments in new facilities and acquisitions over the past two years to create new opportunities for growth.

We continue to balance people and planet with profit.

▲ 27%
$1.3B
REVENUE

▲ 13%
$171.4M
EBITDA

▽ 9%
$75.2M
NPAT

▲ 9%
$203.7M
GROSS PROFIT

▲ 15%
49,180MT
CONSUMER-PACKAGED INFANT FORMULA SALES

▲ 46%
30MT
LACTOFERRIN SALES

*All comparisons in this document are to the 12 months to 31 July 2019 (FY19) unless stated otherwise

ACHIEVEMENTS AT A GLANCE

CORE INFANT BUSINESS CONTINUES TO PERFORM

SYNLAIT POKENO COMMISSIONED

NEW MULTINATIONAL CUSTOMER OPPORTUNITY BEING FINALISED

INVESTMENT IN THE PLANET REMAINS A FOCUS

DAIRYWORKS AND TALBOT FOREST CHEESE ACQUIRED

MANUFACTURING EXCELLENCE CONTINUES

ENGAGEMENT AT RECORD LEVELS

Certified B Corporation

B CORP™ CERTIFIED

MANAGING THROUGH COVID-19 WELL

CHAIR REVIEW

In this, our eighth report to shareholders since we listed the company in July 2013, I am pleased to report that our purpose of *Doing Milk Differently For A Healthier World* has proven its resilience and value when viewed against several significant challenges.

Sadly, the world is not healthier since I last wrote to you. We have all faced extraordinary challenges due to COVID-19. Synlait's purpose was critical to our pandemic response and I am pleased to report that despite COVID-19 we made significant strategic progress and delivered a strong financial performance in the year to 31 July 2020.

A strong result in an extraordinary year

Synlait remains solid and profitable with EBITDA showing our core business is growing strongly, up 13% to $171.4 million. This is however behind the rate originally planned for when we built our new facilities, with customer opportunities taking longer than expected to materialise. NPAT was $75.2 million, which is consequently down on the 2019 financial result, reflecting manufacturing overheads and financing costs absorbed as we invest for future growth.

COVID-19: the opportunity and the challenge for our industry

Synlait is primarily an export-focused company. For that reason, world markets are extremely important to us. Our new reality is that COVID-19 will have a long-term impact on what was a strongly growing world economy until the virus emerged.

Our core business is the manufacturing of essential food to relatively affluent middle classes who can afford optimal nutrition. This is still the case, but when overlaying a global recession and people's ability to afford premium products, sales of high-value items will be impacted to some degree. However, there is no doubt that high-quality, nutritious, sustainable, New Zealand-made products will continue to be in demand.

This situation is not unique to Synlait. In a world challenged economically due to COVID-19, relatively expensive animal and dairy-based proteins will be tested due to consumers reduced buying power. We expect plant-based foods will make headway. We need to monitor trends and be prepared and agile to participate in a way that creates value.

If we look at New Zealand's export story, it is a great platform to operate on – a clean, green image with an excellent record of food quality and safety. The strength of the food and fibre sector, and its importance to New Zealand's economy, was showcased during COVID-19. Despite recent community outbreaks our country has remained relatively COVID-free compared to our global peers. Hopefully, we can keep adding this layer of positivity to Synlait's brand story.

Our internal response to COVID-19 was admirable. Management and employees re-organised early to ensure production would continue in a safe way. Our manufacturing teams were extremely resilient during New Zealand's COVID-19 lockdown with increased demand for fresh milk, cream, cheese and infant formula due to changing consumer behaviours and pantry stocking. We maintained operational and supply chain continuity while responding quickly to our customers changing demand profiles.

This was well supported by our administration team who worked from home. Everyone adapted swiftly and without complaint to working virtually. A testament to Synlait's culture, agility and resilience.

We were therefore well-prepared for the subsequent community outbreak and continue to remain prepared should the virus spread again.

Implementing our strategy

Despite these challenges, Synlait made considerable gains by continuing to implement and execute our strategy throughout the financial year.

To date, our success has been largely based on our core infant nutrition business, which has grown strongly and is integral to our strategy and profitability. On the other hand, the Board and management have the view that we have become too reliant on a single product – infant formula, a single site – Dunsandel, a single market – China, and a single customer – The a2 Milk Company.

We achieved geographical site diversification with the commissioning of Synlait Pokeno. The next phase was to diversify our product range. We needed to attract a customer who would lead us to new markets and categories. While China remains extremely important, we wanted to diversify in terms of geography as well as customer-base.

This process is progressing well and as signaled last month a new, multinational customer opportunity is being finalised.

The Supreme Court appeal regarding Synlait Pokeno was unfortunately necessary this year. We are still awaiting a judgment but remain confident of a favourable outcome. We are pleased this has not impacted our ability to attract a new customer. We consider it unlikely that an adverse decision at the Supreme Court or subsequent proceedings would result in a materially negative impact on our ability to continue to operate Synlait Pokeno.

Perhaps the most notable strategic progress this year was the acquisition of two existing cheese businesses – Talbot Forest Cheese and Dairyworks – as pillars of our Everyday Dairy strategy. This marked the first time we have brought existing businesses into our network. Dairyworks provided us with instant scale in the cheese sector, new growth opportunities, and a diversified earnings base. We are now closer to Australasian consumers and own a fully vertically integrated value chain.

DID YOU KNOW

Dairyworks is a New Zealand leader in the Everyday Dairy category, with a growing Australian presence. It supplies New Zealand consumers with almost half of its cheese, a quarter of its butter, as well as milk powder and ice cream. Learn more at: dairyworks.co.nz

Finally, Synlait's strategic decision to elevate people and planet to the same level as profit was recognised by the company becoming a Certified B Corporation™ (B Corp™) in June. We joined more than 3,300 B Corp™ businesses across 71 countries who have undertaken a stringent assessment process which measures a business's ongoing impact on its workers, community and suppliers, customers, governance and the environment.

DID YOU KNOW

A team of more than 30 Synlait staff were engaged to complete the comprehensive B Impact Assessment. The process took more than a year and Synlait's accreditation will be reviewed every three years. Synlait will use the assessment as stimulus to continue to make positive change within the company.

Refreshing our leadership

In 2019 the Board commissioned a comprehensive review of its capability and succession planning. This highlighted that we have had relatively few Board changes since listing, though in the context of Synlait's rapid growth, stability of representation was considered important.

This is about to change with Bill Roest retiring. Bill joined the Board in 2013 as a highly qualified former Chief Financial Officer and professional Director. He has Chaired the Audit and Risk Committee since joining Synlait and has done a superb job overseeing our capital requirements and bond offers as well as contributing strongly to the overall governance of our company.

The Board will nominate Simon Robertson as its preferred candidate to replace Bill at our annual meeting in November. Simon has extensive executive and governance experience in finance, strategy, risk, operations, technology and stakeholder management. His skills align with Synlait's growth priorities and he is passionate about working in NZX-listed environments having been the former Chief Financial Officer of Auckland International Airport. We hope you will support us in endorsing Simon's Board candidacy.

Under the succession plan, my own term comes to an end next year, and I do intend to stand down and make way for a suitable replacement at that time.

Synlait has continued to develop at a rapid pace. In his second year as CEO, Leon Clement, has certainly responded well to the challenges. The Board is very pleased with his performance, strategic development and leadership.

Leon has also done a great job developing the executive team. While we said goodbye to our former CFO, Nigel Greenwood, Leon has been able to attract and recruit new talent with Angela Dixon (CFO) and Mark Toomey (Director, Operations) joining the team. Angela and Mark bring experience from their careers in significant corporates which will assist Synlait as it enters the next phase of growth.

It has been a challenging year for many reasons. I thank my fellow Directors, our leadership team and employees for stepping up and responding so positively.

Where to from here?

The Board's focus for the next financial year is to continue growing our core infant nutrition business while delivering returns on our investments and diversification initiatives. Having built a world class facility in Synlait Pokeno and seeing a slower growth trajectory than anticipated, we need to ensure our new facilities are fully utilised through new-customer development. We are also focused on the integration of Dairyworks and Talbot Forest Cheese and the commissioning and product verification of Synlait Dunsandel's long-life facility.

Synlait has developed a track record of delivering high returns on capital by investing in a differentiated value chain to meet customer needs, and we are confident that our recent investments will be no different.

We acknowledge that our share price has experienced some pressure as we work to achieve our growth ambitions. The Board remain confident that these investments will drive an improved return for you, our shareholders, over the long-term.

As an essential industry the impact of COVID-19 on supply and demand has not been a severe as on other sectors and therefore the financial performance of Synlait was relatively resilient when viewed against the backdrop of a global pandemic. We do have a strong and profitable business, but we acknowledge there are market headwinds and unused capacity that will restrict our short-term financial performance until fully utilised.

Outlook

There continues to be significant global uncertainty regarding COVID-19.

While Synlait has proven its ability to maintain operational continuity over recent months, in terms of demand for the products it manufactures, it expects:

- Consumer-packaged infant formula volumes to be similar year-on-year, with lower demand in the first half of FY21 due to higher than normal stock levels in the supply chain. Synlait expects a return to growth in the second half of FY21 once stocks have cleared.
- Strong underlying EBITDA and operating cash flows to continue, with growth delivered from a full year of Dairyworks earnings and the integration of Talbot Forest Cheese.
- No disruption to manufacturing or demand for its ingredient and lactoferrin business.

This guidance is subject to the unpredictable effects of COVID-19, with consumer behaviour, channel dynamics and supply chain disruptions all subject to change.

This is offset by the carrying costs of investing in Synlait Pokeno and Synlait Dunsandel's Advanced Dairy Liquid Packaging facility. Earnings from these investments are expected to be delivered in FY22 and beyond.

As previously disclosed, Synlait is in the process of finalising a long-term supply agreement with a new, multinational customer for packaged products which is expected to have a positive impact on earnings from FY23.

Against this, we are targeting a similar, or slight improvement on, our FY20 NPAT result.

A further update will be provided at Synlait's half year result in March 2021.

Thank you for your ongoing support.

Graeme Milne ONZM
Synlait Chair

Milk reception bay, Synlait Dunsandel

CEO REVIEW

Kia ora Synlait whānau

When I reflect on the last financial year it is hard not to think about COVID-19. Organisations can be their most creative in times of uncertainty, and when the future is difficult to predict being adaptable and resilient is an asset. Our team's response to the pandemic was first class, but COVID-19 also confirmed that our strategy to create a strong, diverse company, is more relevant given the uncertain world ahead.

The financial year to 31 July 2020 saw us deliver strong growth in our core business and make genuine progress to further diversify Synlait.

We are building a sustainable, diverse and recurring revenue base that comes from multiple customers, sites, markets and categories, while balancing the needs of people, planet and profit in our decisions.

Strong underlying performance achieved

It was great to see our strong growth momentum continue in this current environment with revenue up 27% to $1.3 billion. EBITDA rose 13% to $171.4 million demonstrating our core business strength, driven by the strong relationship we have with The a2 Milk Company, increased sales from a full year's production from our expanded lactoferrin facilities, and our ability to extract margins from the raw milk we source. We see opportunities to keep growing as the focus on operational efficiency, utilisation and waste reduction continues.

NPAT fell 9% to $75.2 million reflecting strategic investments and acquisitions over the past two years to achieve our diversification ambitions. We acknowledge that a less ambitious strategy may have resulted in a stronger short-term NPAT performance, but it would not have created the growth capacity we now have or addressed our strategic risks.

Yes, we were disappointed when downgrading our performance in February due to changing market dynamics and demand outlook for some of our products. This highlighted our over-reliance on a narrow set of value drivers that can quickly change, again reinforcing the importance of our diversification strategy. Our recovery in the second half, especially given COVID-19, gives us confidence in just how agile and resilient we can be. There are simply too many stories to mention, but I am proud of how our team responded here.

Progressing towards our ambition: 2 + Zero

Our purpose of *Doing Milk Differently for A Healthier World* keeps us on track. Our ambition is a simple formula for success: 2 + Zero. Our goal is to achieve $2 billion in revenue.

The + part of our equation talks to people and planet. Our goal is to have a net positive impact on our environment and communities, and to create a positive place to grow with 100% team engagement. We are balancing people and planet, with profit, in all decisions.

The Zero focuses on a fundamental part of our business – keeping our people safe, our focus on quality, and reducing all forms of loss. Zero injuries, Zero defects and Zero losses. We believe this is possible.

Our progress over the last year towards 2 + Zero was satisfying. Revenue is up 27%, staff engagement is at record levels, we became a Certified B Corporation™, Total Recordable Injury Frequency Rate (TRIFR) is down 38% and our right first-time performance lifted 34%.

Setting the foundations to diversify

In last year's annual report, Synlait was to an extent, one-dimensional. We had an infant nutrition business focused predominantly on our strategic partnership with The a2 Milk Company, and a freshly-inked fresh milk and cream contract with Foodstuffs South Island. We were also reliant on one site, Dunsandel, predominantly manufacturing infant formula for China. Twelve months on we are in better shape.

Customer diversification

We have taken a major step towards achieving a strong, diverse but complementary customer portfolio. In less than two years we have moved from one key relationship to several, creating a well-rounded and long-term customer portfolio, which includes: The a2 Milk Company, a fast-growing player in China; Foodstuffs South Island, a domestic New Zealand retailer; and the new, multinational customer opportunity, that utilises Synlait Pokeno, which we are working to finalise.

These relationships are supported by a balanced portfolio of multinational ingredient and lactoferrin customers, while the Dairyworks and Talbot Forest Cheese acquisitions enable us to connect directly with consumers in a complementary category that help us optimise our milk supply.

Market diversification

We are also broadening our markets effectively. Foodstuffs South Island, Talbot Forest Cheese and Dairyworks provided instant market share in Australia and New Zealand. These markets are experiencing strong sector growth as consumers seek nutritional products that support better health. Synlait is excited to play a role in this journey.

China remains our largest export market. However, there are real, albeit nuanced, shifts happening in the regulatory landscape. We are seeing sentiment shift towards increased consumer trust in Chinese-made infant formula and retail channels, which along with the regulatory landscape, is accelerating market consolidation. This represents opportunity and risk for Synlait, and while we must continuously adapt, we remain highly committed to playing an important role in this critical market with our strategic partner and shareholder The a2 Milk Company.

We are well positioned to continue enabling The a2 Milk Company's growth aspirations via our highly integrated infant formula manufacturing organisation that meets China's high standards. Navigating regulatory environments is core to our value proposition and service. The renewal process required for canned infant formula to be physically sold in Chinese stores every five years is well progressed. New Zealand's reputation as a trusted source of safe dairy nutrition has also been reinforced by our country's response to COVID-19.

Site diversification

We removed our single site and milk pool risk with the commissioning of Synlait Pokeno, some 1,000 kilometres from Synlait Dunsandel. This facility has considerably de-risked Synlait and provides optimisation benefits in the way we manufacture. We now have two infant capable facilities and a1 protein free milk pools at both ends of New Zealand. Synlait Pokeno is a world class facility. Its quality is evidence of our experience built through designing, commissioning and operating these facilities over the past 10 years.

Category diversification

Our core Infant Nutrition category remains solid and profitable. As previously indicated, we are working to finalise a new multinational customer opportunity which expands our category reach.

Our Everyday Dairy strategy made another step forward in April following the Dairyworks acquisition. The focus here is on bringing Talbot Forest Cheese and Dairyworks together to create a uniquely integrated value chain to enhance our market competitiveness and realise synergies.

This category also includes the fresh milk and cream line we operate for Foodstuffs South Island, which we had our first full financial year of sales from. The operational performance of this line is now exceeding expectation and increased demand during COVID-19 was met with almost 100% accuracy. Fresh milk sales rose 2.8% and cream 20% during COVID-19.

Our Foodservice category is being established with the focus on functional UHT whipping creams. Progress was initially delayed due to commissioning challenges on the fresh milk and cream line. Subsequently, commissioning the new UHT line has been further impacted due to COVID-19 as it has been difficult to get the technical capabilities required to New Zealand.

With just over 10 years' experience in producing powdered products, lessons are being learnt and our new Director Operations, Mark Toomey, is using his beverage sector experience to drive this project forward. We remain confident in this opportunity and our strategy. First sales are expected at the end of this financial year.

Our strategic concentration risk has materially reduced over the last year, while maintaining underlying earnings growth in our core business. This approach came with risk as we built in front of the demand curve and acquired complementary businesses, but it is in our DNA to be ambitious and move at pace. We still have work to do, but we have achieved our underlying goal of laying the foundations to build a more diversified Synlait.

Investment in people and the planet: growing in a balanced way

We are pursuing shareholder value creation in a way that enhances the needs of people and the planet. We believe that one drives the other, therefore sustainable thinking is core to what we do. Our investments, and the choices we make, will lead us to being net positive for the planet and help all to thrive.

Our environmental and social progress was recognised in June when we became a B Corp™. We publicly pledged to use business as a force for good and intend to be transparent about our goals and progress towards them. We are committed to creating a future of sustainable farming and integrated food production. This is our core value proposition and we believe it will continue to create value in many ways for our company.

We have some great plans forming to reach our off-farm GHG emissions reduction target of -50% per kilogram of product by 2028. For example, we trialled substituting coal for wood pellets in one of our Dunsandel boilers, which has the potential to remove 30% of the coal we burn.

Whakapuāwai, our native tree planting programme at Synlait Dunsandel, is progressing. The nursery has been constructed and 11,000 trees planted. I am really inspired by our team's commitment to this project. We are truly living Synlait's purpose here.

DID YOU KNOW

Whakapuāwai was launched by Prime Minister Jacinda Ardern in December 2019. Our staff receive one paid day per year to plant natives as a way of supporting commitments to our farmers and communities to jointly restore land in Canterbury.

Our operational response to COVID-19 was also an indicator of our team's commitment to Synlait and a driver of engagement. Those who were needed to run our facilities did so in the knowledge that they were safe and contributing to our company and country's economy. We were privileged to be one of the fortunate few operating as an essential service.

We keep a close watch on engagement with a quarterly measurement programme. We use Gallup's Australia, New Zealand and Oceania database as a benchmark which has seen us move from the 65th to 82nd percentile over the last year, demonstrating our people understand Synlait's purpose and know how to contribute to it.

High engagement correlates to health, safety and wellbeing. In FY18, TRIFR was 18.9 and now it is 8.5. We have work to do, but progress is encouraging. The next step is to ensure a consistent approach at Dairyworks and Talbot Forest Cheese.

Our focus for the year ahead

Our core business is sound and producing solid returns on capital. We are approaching the end of a substantial investment period into manufacturing capacity and people. While this has, for now, had a short-term impact on our bottom line, it has set us up to deliver earnings growth to become a more diversified company. We have the facilities and capability to respond to market opportunities, whether they are new customers, changing consumer tastes, or new products.

To ensure we optimise our performance, we will be focused on three areas this year.

The first is an intense focus on our customer relationships. We must focus on embedding new customer partnerships and continuing to grow existing ones.

The second is the need to fully optimise our assets and create value. We have invested in strategic facilities. It is time to make sure these investments work for us, and you. We are focused on running our facilities smarter and more efficiently.

The third is the simplification and standardisation of our structures and systems. We will continue to build an organisation that is future-ready, and a culture that supports our purpose and ambition.

This is a year to consolidate, focus, and set ourselves up for success. Not all the assumptions we made when we invested in our facilities have played out. Our world has changed, and so must we. We are not going to dwell on what did not work, we are going to do what we need to do to keep creating value for you, our shareholders.

I want to thank those who have been part of the Synlait story.

Our team delivered a strong result in exceptional circumstances. I leave this financial year proud of Synlait, its people and, and our performance.

Ngā manaakitanga

Leon Clement
Synlait CEO

OUR STRATEGY

HEART OUR PURPOSE

DOING MILK DIFFERENTLY FOR A HEALTHIER WORLD

HEAD OUR AMBITION

2

$2 billion in revenue

+

Net +ve impact on
planet and communities
+ve place to grow with
100% engagement

ZERO

Zero injuries
Zero defects
Zero losses

HANDS OUR STRATEGY

DOING MILK DIFFERENTLY

- Sports Nutrition
- Everyday Dairy
- Infant Nutrition
- Foodservice
- Next Big Thing

FOR A HEALTHIER WORLD

- Net Positive for the Planet
- A Healthier Synlait
- World Class Value Chain

DID YOU KNOW

When running at capacity, our Dunsandel and Auckland blending and canning lines tip 6,500 kgs of dry powdered ingredients, including essential vitamins and minerals, per hour into a very large blender to make infant formula.

Blending and canning operator carrying out quality control at Synlait, Dunsandel

HOW WE CREATE VALUE

WHAT WE HARNESS

Natural
Water, energy, land, milk

Social
Customers, farmer suppliers, regulators, community

Human
New Zealand and China-based staff

Strengths-based approach to development

Health and safety leadership

Physical
Owned New Zealand-based assets

Integrated manufacturing systems

Financial
NZX/ASX listings

Long-term strategic shareholder base linked to growth markets

Shareholder capital

Intellectual
Lead with Pride™ programme

Expertise to design, build and operate world-class facilities

Innovation centre

WHAT WE DO

On-farm
Reward New Zealand's most innovative farmer suppliers

Source differentiated milk streams

Operations
Operate world-class facilities

Process differentiated milk streams

Implement best practice food safety, quality and regulatory systems

In-house laboratory

Products
Invest in infant nutrition, ingredients and everyday dairy

Customers
Develop and manufacture specialised products for global brands

Sustainability
Set industry-leading targets and roadmaps

OUTCOMES

Nutritional, safe products
Health and essential nutrition

Trusted brands, product traceability

Extensive product range

Industry challenger
Recognised for on-farm sustainability standards: Lead With Pride™

Catalyst for change

Long-term, high-growth partnerships

Market access
Achieved due to regulatory and quality accreditations

Capability to grow

Talented employees
Innovative and agile culture: Kotahitanga

World-leading engagement results

Safety record improving

Environmental stewardship
On-track to reduce on-farm and off-farm environmental impacts

Certified B Corp™

Financial capability
Lead With Pride™ incentive payments

Competitive margins

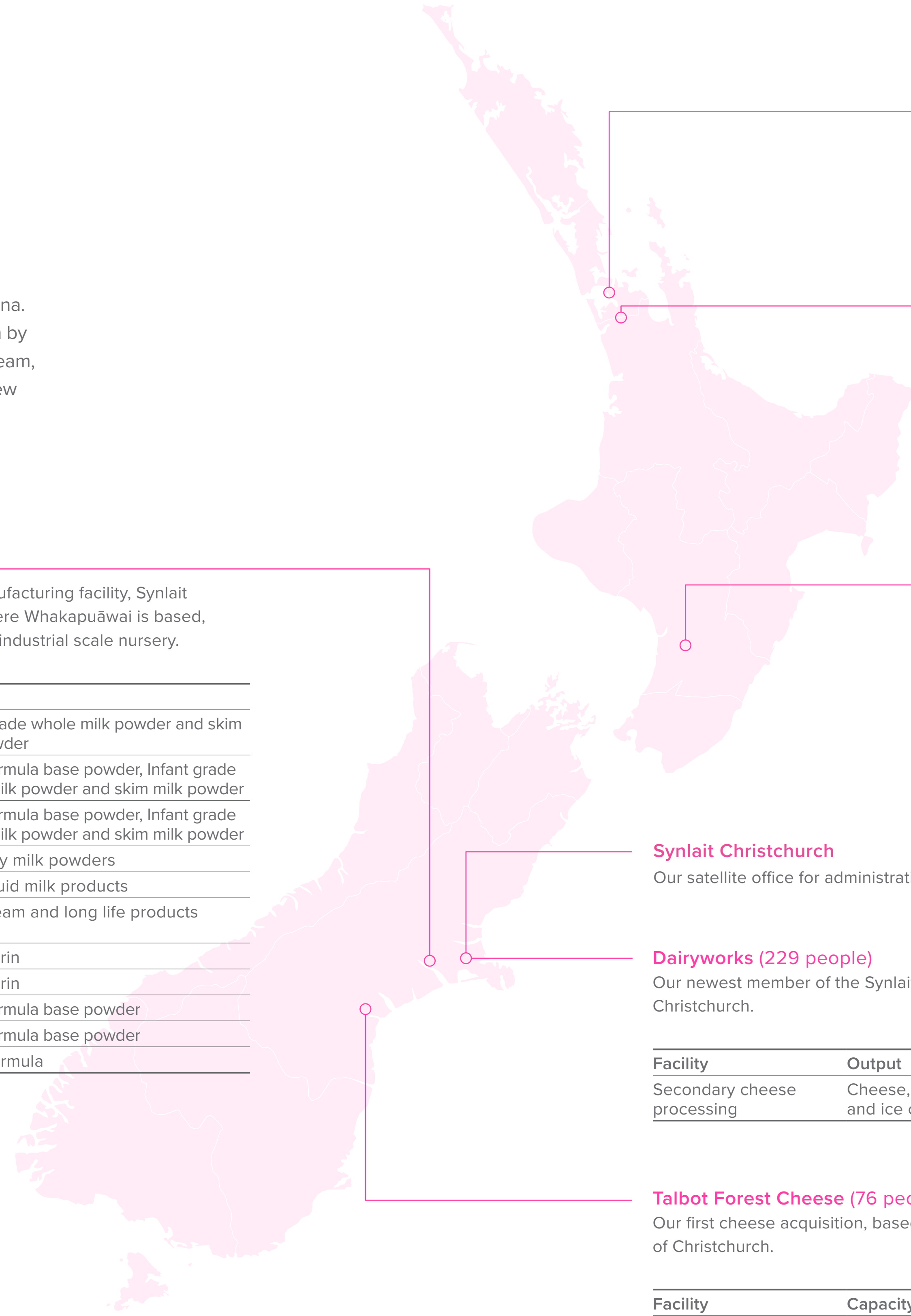
Access to capital for growth

Revenues reinvested

DOING MILK DIFFERENTLY FOR A HEALTHIER WORLD

WHERE WE OPERATE

We have a history of bringing out the best in nature and unlocking its potential through new thinking, new technologies and new attitudes. We have grown to operate across eight locations in New Zealand and China. Our state-of-the-art assets are run by an engaged and highly capable team, backed by some of the best of New Zealand's farmer suppliers.



Synlait Auckland (97 people)

Our second blending and canning facility.

Facility	Capacity	Output
Blending and Canning	40,000 MT	Infant formula

Synlait Pokeno (110 people)

Our newest infant-capable site in the North Island.

Facility	Capacity	Output
Dryer	45,000 MT	Infant formula base powder, Infant grade whole milk powder and skim milk powder
Wetmix Kitchen	45,000 MT	Infant formula base powder, Infant grade whole milk powder and skim milk powder

Synlait Palmerston North (17 people)

Our research and development centre based at Massey University.

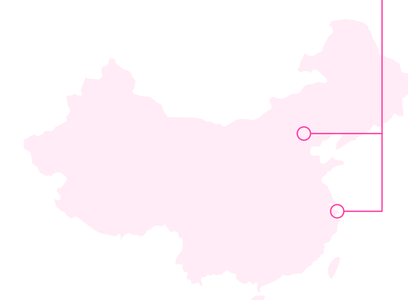
Synlait Dunsandel (838 people)

Our homebase. As well as being our primary manufacturing facility, Synlait Dunsandel has an administration office and is where Whakapuāwai is based, our environmental programme which includes an industrial scale nursery.

Facility	Capacity	Output
Dryer 1	45,000 MT	Infant grade whole milk powder and skim milk powder
Dryer 2	45,000 MT	Infant formula base powder, Infant grade whole milk powder and skim milk powder
Dryer 3	45,000 MT	Infant formula base powder, Infant grade whole milk powder and skim milk powder
SMD	1,800 MT	Specialty milk powders
AMF	25,000 MT	AMF liquid milk products
Advanced Dairy Liquid Packaging Facility	110ML	Milk, cream and long life products
Lactoferrin 1	17 MT	Lactoferrin
Lactoferrin 2	17 MT	Lactoferrin
Wetmix Kitchen 1	40,000 MT	Infant formula base powder
Wetmix Kitchen 2	45,000 MT	Infant formula base powder
Blending and Canning	40,000 MT	Infant formula

Synlait China (6 people)

Our teams in Shanghai and Beijing are focused on regulatory affairs, business development and sales.



Synlait Christchurch

Our satellite office for administration staff.

Dairyworks (229 people)

Our newest member of the Synlait family based in Christchurch.

Facility	Output
Secondary cheese processing	Cheese, butter, yogurt, milk powder and ice cream

Talbot Forest Cheese (76 people)

Our first cheese acquisition, based in Temuka, two hours south of Christchurch.

Facility	Capacity	Output
Primary cheese manufacture	12,000 MT	Cheese

DID YOU KNOW

80% of our South Island farmer suppliers are within a 75 kilometre radius of Synlait Dunsandel.

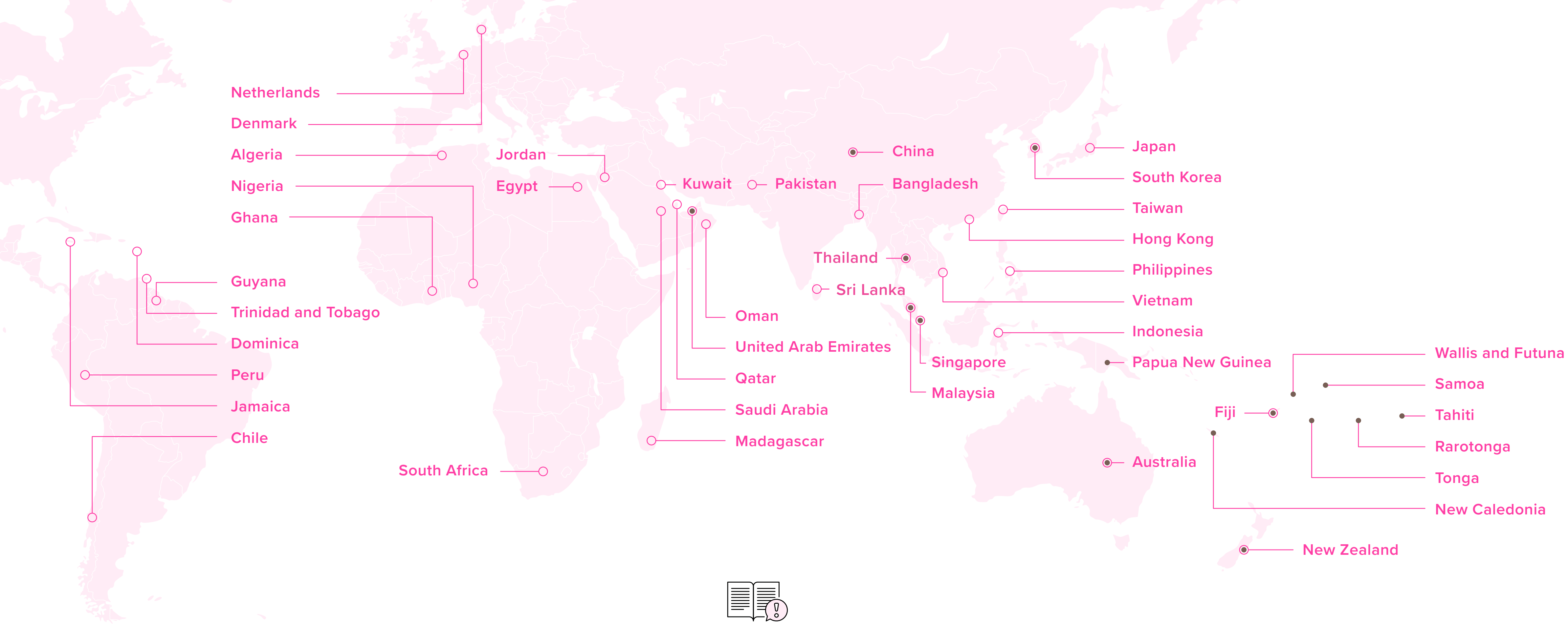
80% of our North Island farmer suppliers are within a 130 kilometre radius of Synlait Pokeno.

WHERE OUR MILK GOES

Our differentiated milk supply is what sets Synlait apart. It enables us to manufacture a range of nutritional milk products that provide genuine benefits for human health and wellbeing for our global customers. New Zealand's unique environment is reflective of the quality of the milk we produce, and our milk finds its way all over the world.

KEY: DISTRIBUTION BY COUNTRY

- ○ Synlait manufactured
- • Dairyworks manufactured



DISTRIBUTION BY PRODUCT

	Countries exported to
Synlait	
Anhydrous milk fat	21
Butter milk powder	3
Consumer packaged infant formula	3
Infant formula base powder	3
Lactoferrin	4
Skim milk powder	17
Whole milk powder	23
Dairyworks	
Cheese	20
Flavoured butter	1
Ice cream	18
Salted and unsalted butter	18
Whole milk powder	16

DID YOU KNOW

Commercial product, including instant whole milk powder, skim milk powder, infant formula base powder and cream, has been manufactured at Synlait Pokeno since September 2019. The first shipment of whole milk powder was dispatched in December 2019 to Vietnam.

WHAT MATTERS MOST TO OUR STAKEHOLDERS AND TO OUR BUSINESS

To improve as an organisation we need to identify, understand and closely manage our performance on the topics that are most material to us and our stakeholders.

This year we performed a desktop materiality assessment, reviewing reports from suppliers, customers, investors and other external stakeholders to assess relevant issues that can affect value.
The outcomes of the materiality assessment inform our decision making on where we aim to make an impact and feed into our corporate reporting framework.

The materiality assessment focuses on those topics that are most relevant or impactful for the company and its stakeholders, covering economic, social, and environmental topics.

Working from a long list of topics, a shortlist was created for further discussion with internal stakeholders to assess their views on Synlait's impact and to find out which subjects are important for our stakeholders.

The topics with the highest priority for stakeholders and the biggest estimated impact on our business or on society appear in this matrix. All topics shown in the top right corner of the chart are considered material and high priority. Our goal is to refine this materiality analysis and matrix by interviewing external stakeholders over the coming years.

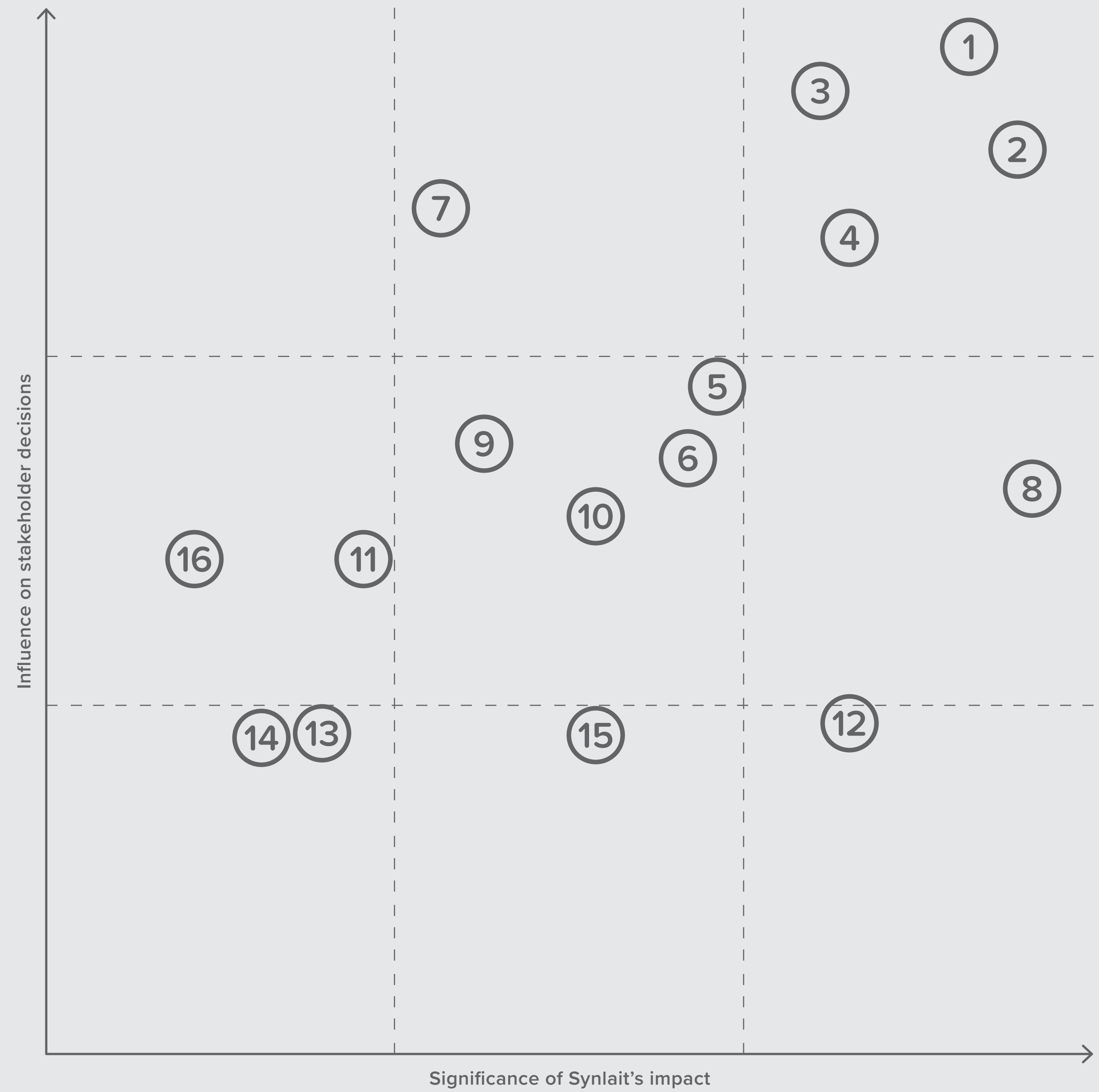
LEARN MORE

More information on our risk management framework can be found in the Corporate Governance section of this report on page 133.

MATERIAL TOPICS

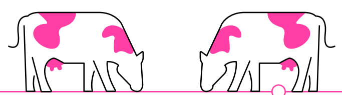
1. Food safety
2. Animal welfare
3. Water quality
4. Climate change
5. Safety and wellbeing of employees
6. Land degradation
7. Customer diversity
8. Market access / geopolitical unrest
9. Plant-based foods / innovation
10. Product provenance and traceability
11. Plastic packaging, waste, reuse and recycling
12. Social responsibility
13. Nutrition
14. Recessionary conditions / Net debt risk and return on investment
15. Cyber security
16. Organisational capability and culture

MATERIALITY MATRIX



TWO DECADES OF PROGRESS

THE SYNLAIT STORY 2000 - 2020



2000

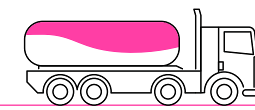
The Synlait dream begins

Dairy farmers and entrepreneurs Ben Dingle, Juliet Maclean and Dr John Penno purchased Robindale Dairy Farm in Canterbury.

2005

Synlait is formed

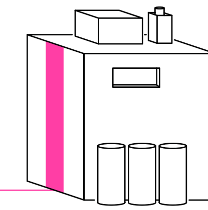
Synlait Milk launched. The name Synlait was derived from the words 'synergy' and 'lait' (French for milk).



2007

The Synlait Dunsandel dream begins

Synlait Milk entered an agreement to deliver all milk collected to Westland Milk Products during construction of Dryer 1.



2008

First milk processed at Synlait Dunsandel

In June Synlait Dunsandel received its first milk from third-party farmer suppliers.

Dryer 1 was commissioned in August and the Anhydrous Milk Fat facility was commissioned in September.

2009

Development continues at Synlait Dunsandel

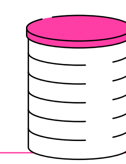
The special milks spray dryer was commissioned in August.

2010

Bright Dairy joins the Synlait family

Bright Dairy invested capital in Synlait Milk and became a 51% shareholder in November.

Synlait Dunsandel commenced construction of Dryer 2, a sophisticated purpose-built infant formula facility.



2011

First milk processed in Synlait Dunsandel's infant formula facility

On 15 September the first milk was processed in Synlait Dunsandel's infant formula facility.

Dryer 2 is commissioned. Synlait Milk has the capability to manufacture infant formula and nutritional products to unique customer specifications.

2012

Supply agreement signed with the A2 Corporation Limited

In March, an agreement was signed with A2 Corporation Limited (later known as The a2 Milk Company™ Limited) for Synlait Milk to process and supply The a2 Milk Company™ Limited's a2 Platinum® infant formula.

2013

A big year for Synlait

In April, Synlait Milk launched its internationally accredited ISO/IEC 17065 dairy farm assurance programme, Lead With Pride™, which recognises and financially rewards farmer suppliers who achieve dairy farming best practice.

On 23 July Synlait Milk Limited listed on NZX, New Zealand's Exchange.

2014

New facilities come on-line

At Synlait Dunsandel, the Lactoferrin extraction and purification facility was commissioned in April and the blending and consumer packing facility in July. Also, in July, Dry Store 3 was completed.

2015

Synlait Dunsandel upgrades continue

Dryer 3, an infant formula grade spray dryer, was commissioned in September at Synlait Dunsandel.

2016

Capital raising and ASX listing

In October, Synlait Milk completed a $98 million capital raise.

Synlait Milk Limited listed on the Australian Securities Exchange (ASX) on 25 November.

2017

Focused on growth

Synlait Auckland, a blending and consumer packaging facility, was commissioned in November. This was formerly the site of The New Zealand Dairy Company Limited, which Synlait Milk purchased in May that year.

The Wetmix kitchen at Synlait Dunsandel was officially opened in December, doubling Synlait's infant formula powder capacity.

2018

Celebrating 10 years of operations ...

In February, Synlait announced the conditional purchase of 28 hectares of land in Pokeno, North Waikato to establish its second nutritional power manufacturing site.

This was followed by the official opening of the Synlait Research and Development Centre in Palmerston North, a partnership with Massey University and Food HQ, in March.

In August, Dr John Penno, founder and former Managing Director stepped down from the role of CEO, and Leon Clement was appointed.

Synlait announced bold 10-year sustainability targets in September and launched a new corporate brand identity and purpose *'Doing Milk Differently For A Healthier World'* in November.

Construction of the Advanced Dairy Liquid Packaging Facility commenced at Synlait Dunsandel.

2019

Synlait continues to grow and grow ...

New Zealand's first large-scale electrode boiler was commissioned at Synlait Dunsandel in March. This was a significant social and environmental performance milestone for Synlait Milk.

Synlait Milk commenced supply of fresh liquid milk and cream to Foodstuffs South Island in April from its newly commissioned Advanced Liquid Dairy Packaging Facility at Synlait Dunsandel.

The acquisition of selected assets of Talbot Forest Cheese was completed in August. This acquisition supported Synlait Milk's broader growth and diversification strategy.

Synlait Milk announced in September that revenue exceeded $1 billion for the first time in the company's history.

Synlait Pokeno processed its first milk in September.

Lactoferrin facility expansion at Synlait Dunsandel commissioned in October, doubling the manufacturing capacity.

Whakapuāwai programme and electrode boiler officially opened by the Prime Minister at Synlait Dunsandel in December.

Synlait Milk listed $180 million subordinated bonds on NZX's Debt Market in December.

2020

Twenty years on and the focus on growth continues

Synlait Milk became the owner of Dairyworks Limited in April.

Synlait Milk became a Certified B Corporation™ in June.

Synlait Milk acquired farmland adjacent to Synlait Dunsandel. The land will enable Synlait Milk to pursue several strategic supply chain and sustainability initiatives that support Synlait Dunsandel's long-term operation and expansion.

Dry Store 4 during construction shortly after the roof was completed in August 2020

DRY STORE 4

Dry Store 4 will provide an additional 30,000 square metres of warehousing at Synlait Dunsandel. It will streamline logistics activities and bring offsite South Island storage back to Dunsandel, supporting growth and generating supply chain efficiencies. It enables greater control over our inventories, value add services, improves our sustainability footprint, and improves lead times for our customers. New technology and infrastructure improvements will enhance the health and safety of our people too. It will be completed in November 2020.

OUR BOARD

Graeme Milne ONZM (Chair)

Bill Roest

Dr John Penno

Min Ben

Qikai Lu

Hon. Ruth Richardson

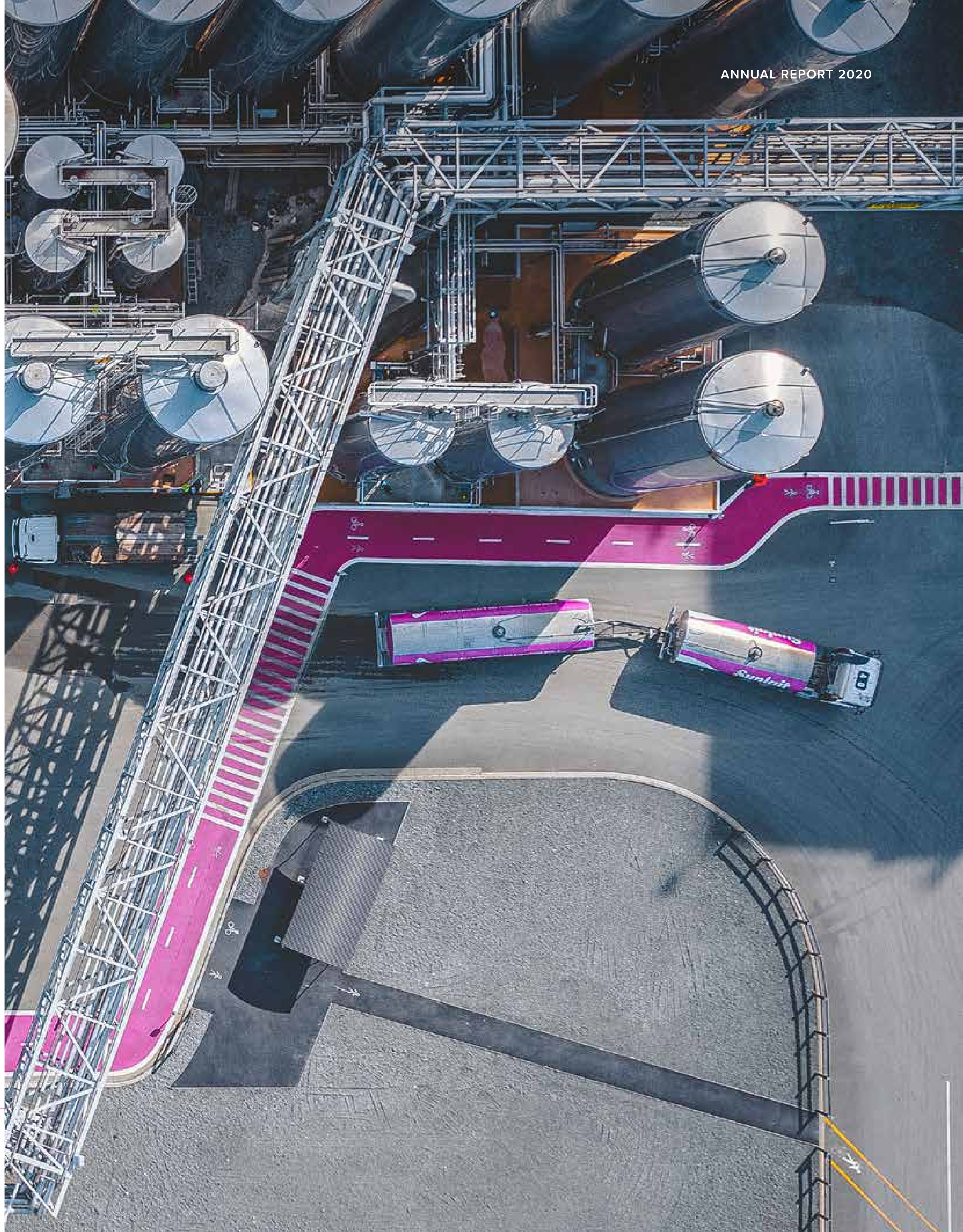
Sam Knowles

Sihang Yang

LEARN MORE

The Board's full profiles are available on our website: synlait.com/people

Other information about Board composition and performance is disclosed in the corporate governance section on page 133. Information on Directors remuneration, participation in Synlait securities, and other interests are disclosed in the statutory information section on page 153.



The pink health and safety pathway at Synlait Dunsandel

OUR EXECUTIVE TEAM

Leon Clement
Chief Executive Officer

Angela Dixon
Chief Financial Officer

Boyd Williams
Director, People, Culture and Performance

Chris France
Director, Strategy and Business Transformation

Deborah Marris
Director, Legal, Risk and Governance

Hamish Reid
Director, Sustainability and Brand

Mark Toomey
Director, Operations

Martijn Jager
Director, Sales and Business Development

Dr Suzan Horst
Director, Quality, Regulatory and Laboratory Services

LEARN MORE

The Executive Team's full profiles are available on our website:
synlait.com/people

Milk reception bay, Synlait Dunsandel

A Synlait Dunsandel warehouse operator loads an order of fresh milk and cream from the coolstore for delivery to Foodstuffs South Island stores

FOODSTUFFS SOUTH ISLAND

"During New Zealand's COVID-19 Alert Level 4 lockdown we saw a significant increase in consumer demand for fresh milk and cream across the South Island. The Synlait team pulled out all stops to deliver on our unscheduled requirements – this is a testament to the solid relationship we have developed."

Phil Lemon, GM Merchandise, Foodstuffs South Island

CFO REVIEW

Angela Dixon joined Synlait as Chief Financial Officer in June 2020. She has more than 20 years' experience in the financial, professional services and insurance sectors in New Zealand and the United Kingdom, holding senior roles with Public Trust, IAG, Auckland International Airport, Telewest Communications, Royal Sun Alliance and PwC.

FIRST IMPRESSIONS FROM OUR NEW CFO

I am a recent recruit to Synlait's Executive Leadership Team and this, my first report to you, our shareholders, provides a unique opportunity to introduce myself and share some first impressions of our business.

Although I come from a background in corporate finance and insurance, I know the dairy industry well. I grew up on a dairy farm in the Waikato, gaining a first-hand appreciation of how our industry worked, including watching the creation of Fonterra Co-operative Group unfold over the years as a result of many mergers around us.

Our farm was not far from the Tatua Co-operative Dairy Company catchment, and we were very aware of the successes of Tatua as it was evidence of the virtues of being small and competitive. Because of this, I was attracted to the proposition of Synlait as a challenger who is showing the industry how to do milk differently.

I was also attracted to Synlait's sustainability story. Coming from an extended family of dairy farmers, we were encouraged to respect and care for the land. My family believed in being sustainable, competitive and nimble. These values were instilled in me. I am a passionate and proud New Zealander who wants to contribute to a more sustainable world. Synlait is a change-maker influencing the food and fibre industry for the better. I am excited to be part of this journey.

Getting fit and ready for the next phase of growth

Through the recruitment process I discovered Synlait had grown to be larger than meets the eye. This is when I realised my skill set would benefit Synlait. I have spent my career working for large corporate organisations and have experience working through complexity to find simplicity.

Synlait has had a successful run up the curve, but we are no longer a start-up. We are a significantly sized company by New Zealand standards, operating across multiple sites and countries. We must navigate how we will continue to grow with a maturing company mindset, without losing the entrepreneurial spirit we were founded on.

I do not have manufacturing experience, but I know that every dollar is hard won in a mature market. You must watch costs and margins closely. I also bring experience in diversifying businesses. When you buy another company, you need to realise value and deliver the results quickly. Synlait is experiencing this with Dairyworks. We will integrate it strategically, while showing you the value we are creating by owning it.

We are taking Synlait to the world

Synlait's brand and reputation have enabled it to attract intelligent people. I am impressed by the culture. Our team is full of fresh and optimistic people who care about being part of this organisation and see the growth possibilities. We are attracting global talent because of this.

Synlait has done the hard yards. It has built first-class facilities. It has world-class expertise in manufacturing and exporting. It is partnered with successful brands and provided quality products repeatedly. Now, we need to pivot to partner with more customers.

There are natural constraints right now due to COVID-19, and our current and potential customers are being rightly cautious. But the pandemic will not destroy the value already invested into Synlait. We have the building-blocks in place – the facilities, the expertise, the partnerships and market intelligence. The future for Synlait is about how we accelerate and fully utilise those building-blocks to keep growing.

Thank you for making me feel welcome. I look forward to continuing to hear your perspectives on Synlait as I build my knowledge of our company and industry.

Angela Dixon
Chief Financial Officer

FINANCIAL AND PERFORMANCE METRICS

Key financial metrics [1] Currency as stated (in millions)	FY2016	FY2017	FY2018	FY2019	FY2020
Income statement					
Revenue	546.9	759.0	879.0	1,024.3	1,302.0
Gross profit	102.1	112.1	166.5	186.3	203.7
EBITDA [2]	83.7	88.8	138.6	152.1	171.4
EBIT [2]	62.9	67.6	113.1	124.5	123.3
NPAT	**35.7**	**39.5**	**74.6**	**82.2**	**75.2**
Revenue (USD per MT) [3]	3,316	3,659	4,815	4,602	5,181
Gross profit per MT (NZD) [3]	877	792	1,294	1,268	1,359
EBIT per MT sold (NZD) [3]	540	478	879	855	858
Net cash from / (used in) operating activities	**104.4**	**115.2**	**98.4**	**136.7**	**105.5**
Balance sheet					
Net operating assets [4]	455.2	423.5	493.3	633.9	1,043.3
Return on net operating assets	16.2%	15.4%	24.7%	22.1%	14.7%
Net return on capital employed (pre-tax)	14.5%	14.8%	22.7%	18.3%	12.6%
Debt / debt + equity (excl derivatives)	48.7%	18.7%	20.9%	39.2%	47.1%
Net debt / EBITDA[6]	2.5	0.9	0.8	2.2	3.1
Earnings per share	**23.50**	**22.82**	**41.60**	**45.89**	**41.95**
Average FX conversion rate (NZD:USD)	**0.7058**	**0.6814**	**0.7047**	**0.6792**	**0.6651**
Base milk price	3.91	6.16	6.65	6.40	7.05
Total milk price (kgMS)[5]	**4.02**	**6.30**	**6.78**	**6.58**	**7.30**
Key operational metrics					
Sales (MT)					
Powders and cream	100,393	122,606	93,042	106,802	101,222
Consumer packaged Infant Formula	15,999	18,776	35,580	42,907	49,180
Lactoferrin	10	11	16	21	30
Total sales (MT)[3]	**116,402**	**141,393**	**128,637**	**149,730**	**150,432**
Production (net production)					
Powders and cream	104,703	115,991	102,833	103,131	107,098
Consumer packaged Infant Formula	16,043	19,403	36,651	43,168	50,918
Lactoferrin	8	12	12	23	29
Total production (MT)[3]	**120,754**	**135,407**	**139,496**	**146,322**	**158,045**
Milk purchases ('000 kg MS)					
Milk purchased from contracted supply	54,125	63,255	63,639	64,189	76,875
Milk purchased from other suppliers	3,573	1,700	(2,853)	1,877	(6,079)
Total milk purchases ('000 kg MS)	**57,698**	**64,954**	**60,785**	**66,066**	**70,796**

[1] The group uses several non-GAAP measures when discussing financial performance. Management believes these measures provide useful insight on the performance of the business, to analyse trends and to assist stakeholders in making informed decisions.

[2] EBIT is calculated by excluding financing costs and income tax, with EBITDA also excluding depreciation & amortisation accordingly. A reconciliation of EBIT and EBITDA is provided in the CFO Review on page 49.

[3] Synlait Milk Limited only and fresh milk is excluded in FY20 and FY19 (part year in FY19)

[4] Net operating assets includes current assets, PPE and intangible assets. It excludes capital work in progress, derivatives, goodwill, trade payables and tax liabilities.

[5] Total milk price for Synlait Milk suppliers on standard milk supply contract, includes value and seasonal premiums. This is a milk season reflective payment that runs 1 June to 31 May.

[6] Net debt calculation excludes lease liabilities, for banking covenant purposes lease liabilities are included.

MILK PRICE

This table shows how Synlait take the milk supplied by our contracted farmer suppliers, value the milk components, and make a pay-out via the average base milk price.

The 2019/20 milk price had not been fully paid out at the time the annual report was released. Figures represent what has been paid and is accrued to be paid.

It also highlights the incentive payments made to our farmer suppliers in addition to the average base milk price.

This information represents payments made in the milk season which runs 1 June to 31 May as opposed to Synlait's financial year.

For the recently completed 2019/2020 milk season we paid out an average base milk price of $7.05 with an average additional incentive payment of $0.25 per kgMS.

	2016/17	2017/18	2018/19	2019/20
kgMS collected	63,249,602	63,616,077	63,438,694	76,550,913
Average fat %	4.90	4.86	4.91	4.90
Average protein %	3.92	3.89	3.92	3.98
Average lactose %	5.06	4.99	4.99	4.99
Volume of components collected (kg)				
Fat	35,123,275	35,289,377	35,270,506	42,252,084
Protein	28,126,327	28,327,076	28,168,188	34,298,829
Lactose	36,292,742	36,221,310	35,894,766	42,977,611
Component value[1]				
Fat	$4.70	$6.97	$7.36	$8.44
Protein	$6.56	$4.63	$4.18	$4.20
Lactose	$1.87	$2.03	$1.53	$1.67
Component value ratio				
Fat	1	1	1	1
Protein	1.397	0.664	0.567	0.497
Lactose	0.398	0.291	0.208	0.198
Total $ paid per component				
Fat	$164,998,609	$245,903,402	$259,645,339	$356,688,641
Protein	$184,528,391	$131,063,290	$117,657,713	$143,911,349
Lactose	$67,823,876	$73,377,129	$54,987,988	$71,818,527
Volume charge	($27,732,308)	($27,289,173)	($26,283,402)	($32,746,784)
Average base milk price[2]	**$6.16**	**$6.65**	**$6.40**	**$7.05**
Total incentive payment	$8,908,367	$8,127,045	$11,530,895	$19,249,791
Average incentive payment per kgMS[3]	$0.14	$0.13	$0.18	$0.25
Total average Synlait payment per kgMS[4]	**$6.30**	**$6.78**	**$6.58**	**$7.30**

[1] Rounded to two decimal places

[2] Amount paid for components + volume charge / kgMS collected = base milk price

[3] Includes incentives and winter incentive payments

[4] Base milk price + average incentive payment

REVIEW OF FINANCIAL PERFORMANCE

OVERVIEW

The Group has continued to execute on its strategy of growing both our Nutritional (infant and lactoferrin) and Everyday Dairy businesses which is reflected through revenues exceeding $1 billion for the second time in FY20 with revenues of $1,302.0 million. Earnings before interest, tax, depreciation and amortisation (EBITDA) grew 13% to $171.4 million demonstrating the strength of our infant and lactoferrin businesses. Reported after tax earnings were a profit of $75.2 million, a 9% decrease reflecting investments in new facilities and acquisitions over the past two years to achieve growth ambitions as well as increased overhead expenditure in areas of the business that support future growth opportunities aligned to our strategy.

FINANCIAL PERFORMANCE

Sales

Revenue in FY20 at $1,302.0 million is $277.7 million or 27% higher than FY19 ($1,024.3 million), with total sales volume of 150,432 MT (excluding Everyday Dairy, which is discussed in a separate section below) in line with FY19 but product mix significantly moving from commodities to higher value canned infant formula.

This revenue growth was driven by a 15% increase in high value canned infant formula sales, and a 46% increase in lactoferrin sales volumes. The uplift in higher value product sales was enabled by the investments made in prior years as well as from manufacturing efficiencies which have delivered through our Integrated Work Systems (IWS) programme.

Sales (metric tonnes)	FY20	FY19	Growth %
Ingredients	101,222	106,802	(5)%
Consumer packaged powders	49,180	42,907	15%
Lactoferrin	30	21	46%
Total	150,432	149,730	0.5%

We received 76.8 million kilograms of milk solids (kgMS) from our contracted suppliers, 12.4 million kgMS more than FY19 to support the Pokeno facility. We also sold (net) 6.0 million kgMS over the season of which 1.4 million kgMS was cream sold from the Pokeno facility, resulting in an overall 7% or 4.4 million kgMS increase in milk processed in FY20. Again, this was enabled by the investments and implementation of the IWS programme as mentioned above – the IWS programme increased facility production capacities validating the investment management has made into this programme.

Average reference commodity prices increased steadily in the first half of the 2019/20 milk season until February. Reference commodity prices fell steadily from February through May as global uncertainty driven by COVID-19 impacted commodities. The average reference basket price in the 2019/20 season increased to $3,128, a 4% increase vs the 2018/19 season. This increase, as well as a lower FX rate, are the key contributors to the $0.65 increase in the average base milk price paid to our suppliers in 2019/20, which moved from $6.40 to $7.05 per kgMS.

Gross profit performance

Sales

Our total gross profit per MT of $1,359 is 7% higher than last year's $1,268 per MT. A direct result of the favourable sales product mix in FY20. Continued investment in people to support key growth projects, higher Lead With Pride™ supplier engagement costs, and the full impact of depreciation from the completion of the investment program in prior years tempering the upside. Over time, as we grow into our capacity, we will see a positive incremental impact on gross profit and increased ROCE with fixed costs per MT at its highest immediately after the completion of a new facility.

Consumer packaged gross profit improved $24 per MT, generated from higher utilisation of our consumer packaging facilities in Dunsandel and Auckland.

Lactoferrin margin per MT has materially increased over FY19 due to a favourable market pricing environment. Lactoferrin production volume also increased following the facility upgrades which were completed in November 2019 (up 26%), and overall contributed $28 million of gross profit in FY20 (FY19: $13 million).

Everyday Dairy

The Everyday Dairy category represents the acquisition of Talbot Forest Cheese and Dairyworks, along with the Advanced Dairy Liquid Packaging Facility at Dunsandel. Gross Profit from this area is net $0.4 million, a result reflecting some initial commissioning challenges in the Advanced Dairy Liquid Packaging Facility at Dunsandel and low fixed overhead recoveries as we move from commissioning phase to a focus on increasing utilisation. Dairyworks and Talbot Forest Cheese are tracking to expectations generating Gross Profit of $2.6 million combined in FY20. In FY21 we will focus on integrating Dairyworks and Talbot Forest Cheese and leverage synergies with the core Synlait business.

Gross profit by category[1]

		Powders and Cream	Consumer Packaged Infant Formula	Lactoferrin	Total Powders
	Sales Volume (MT)	101,222	49,180	30	150,432
FY20	Gross Profit ($M)	134.4	40.5	28.4	203.3
	Gross Profit / MT	1,327	824	943,074	1,359
	Sales Volume (MT)	106,802	42,907	21	149,730
FY19	Gross Profit ($M)	142.2	34.3	13.3	189.8
	Gross Profit / MT	1,331	800	646,099	1,268
	Sales Volume (MT)	(5%)	15%	46%	0%
% Change	Gross Profit ($M)	(6%)	18%	113%	7%
	Gross Profit / MT	0%	3%	46%	7%

[1] Gross profit per MT includes both external sales volumes and internal transfers of bulk infant formula to blending and consumer packaging.

Milk price

Raw milk remains Synlait's most significant component of our cost of goods sold. Our final average base milk price for the 2019/20 season is $7.05 per kgMS, compared to our 2018/19 average base milk price of $6.40 per kgMS. In addition, we paid out $0.25 per kgMS in incentive and premium payments through a2, Lead With Pride™, Grassfed and winter milk payments, increasing the average total milk payment to $7.30 per kgMS compared with $6.58 per kgMS in 2018/19. Premiums and incentive payments are higher in 2019/20 predominantly through an increase in our winter milk payments. This resulted in our contracted suppliers receiving a total of $19.3 million in additional value-added premiums in the 2019/20 season, compared to $11.5 million in 2018/19.

Overhead expenditure

Overhead expenses for FY20 at $80.9 million were up $18.7 million from $62.1 million in FY19. Notable increases in these overhead costs include overhead expenditure from acquired subsidiaries ($4.6 million), depreciation ($4.0 million), employee costs ($4.4 million) and multi-site distribution ($1.4 million).

As previously signalled, increases in overhead expenditure reflect continued investment to help run the new facilities that we are bringing on-line and enter new categories.

The impact of COVID-19 on expenditure is not evident in the year-on-year comparison. However, there was a reduction in training, entertainment, travel and consulting costs totalling $2.5 million across the business. This is partially offset by higher cleaning costs of $0.3 million and additional warehouse space costs of $0.2 million to mitigate against the risk of export channels slowing down.

EBITDA

Earnings before interest, tax, depreciation and amortisation (EBITDA), at $171.4 million, grew strongly demonstrating the strength of our infant nutritional and lactoferrin businesses. The 13% increase on the FY19 result of $152.1 million was driven by increased sales volumes and a favourable product mix.

$ million	FY20	FY19
Profit before tax	$101.9	$115.1
Add back: net finance cost	$21.4	$9.4
EBIT	**$123.3**	**$124.5**
Add back: depreciation and amortisation	$48.1	$27.6
EBITDA	**$171.4**	**$152.1**

Net financing costs

Net financing costs at $21.4 million increased 127% over FY19's $9.4 million.

	FY20	FY19	Var.
Gross term debt interest	(15.2)	(9.4)	(5.8)
Less capitalised interest	2.1	7.5	(5.4)
Net term funding interest	**(13.1)**	**(1.9)**	**(11.2)**
Working capital funding interest	(6.2)	(6.9)	0.7
Interest received	0.1	1.2	(1.1)
Loss on derecognition of financial assets	(1.7)	(1.8)	0.1
Net short-term funding interest	**(7.8)**	**(7.5)**	**(0.3)**
Interest on lease liabilities	(0.5)	0.0	(0.5)
Net finance costs	**(21.4)**	**(9.4)**	**(12.0)**

The $12.0 million increase in net financing costs is due to an increase in interest-bearing debt as a result of continued capital expenditure and lower capitalised interest.

Gross interest on term debt increased by $5.8 million to $15.2 million in FY20 with higher average interest-bearing debt year-on-year as a result of the acquisition of subsidiaries and continued capital expenditure across both years, with lower interest rates providing some offset. Capitalised interest decreased by $5.4m to $2.1m in FY20 with Synlait Pokeno commissioned in early FY20 and the Advanced Dairy Liquid Packaging Facility at Dunsandel commissioned in FY19.

Working capital funding interest has decreased by $0.7 million due to lower interest rates, partly offset by higher working capital requirements in FY20 than in FY19. Those working capital requirements being Synlait's continued growth; inventory build of infant nutritional products to ensure customer demand is able to be met, to protect against COVID-19 supply chain disruption, and to ensure optimal utilisation of our plant through peak milk collection; together with the additional working capital requirements of Dairyworks and Talbot Forest Cheese, which were acquired in FY20.

Loss on derecognition of financial assets is the financing cost associated with our receivables financing programme. It has decreased slightly with lower interest rates offset by increased utilisation of these facilities.

Further, the Group adopted NZ IFRS 16 effective from 1 August 2019, resulting in $0.5m interest on lease liabilities for FY20 (FY19: nil).

Foreign Exchange

The management of foreign exchange exposure is one of the key risks of the business with many product sales being to overseas markets creating a primarily United States Dollar (USD) exposure risk. Our foreign exchange policy seeks to achieve the lowest annual average New Zealand Dollar (NZD)/USD exchange rate for the year. In FY20 we achieved a net annual average NZD/USD exchange rate of 0.6651 (FY19: 0.6792).

Earnings per share and return on capital employed

Our reported basic and diluted earnings per share (EPS) for FY20 was 41.95 cents and 41.85 cents respectively, against 45.89 cents and 45.77 cents in FY19. The dilutive shares are basic EPS adjusted for contingently issuable shares in accordance with the Employee Share Scheme. The Group also generated a pre-tax return on average capital employed of 12.6% in FY20 compared with 18.3% in FY19.

FINANCIAL POSITION

Overview

In FY20 the Group continued to invest for the future, completing the construction of assets and acquisition of businesses to allow us to successfully implement our strategy.

Our reported net profit after tax of $75.2 million, plus the movement in reserves, has increased total equity to $606.5 million at 31 July 2020 from $492.4 million.

Trade and other receivables

At $63.1 million, Group trade and other receivables have increased by $1.2 million on FY19 ($61.9 million). Synlait's trade and other receivables have decreased significantly year on year to $36.1m (FY19: $61.9m) driven by an increased balance of receivables assigned as at 31 July 2020 (FY20: $131.3, FY19: $109.0). The differential is the trade and other receivables of the subsidiaries acquired during FY20 (Dairyworks and Talbot Forest Cheese).

Inventories

Our inventory holdings increased to $269.4 million (FY19: $164.8 million). $53.3 million of this increase relates to the inventory holdings of subsidiaries acquired during the year. The balance of the increase at Synlait is largely due to increased holdings of canned and bulk infant nutritional products to ensure customer demand is able to be met, to protect against potential Covid-19 supply chain disruption (increased safety stock), and to ensure optimal utilisation of our plant through peak milk collection in FY21.

	FY20		FY19	
	$ million	MT	$ million	MT
Synlait Milk Limited	216.1	40,787*	164.8	34,625*
Dairyworks Limited	40.1	4,889*	-	-
Synlait Foods (Talbot Forest) Limited	13.2	1,766	-	-

* inventory not measured in metric tonnes is excluded as not material to our volumes.

Raw materials increased to $71.3 million (FY19: $40.1 million). Tonnage of raw materials increased to 13,614 (FY19: 11,307 MT). Higher raw materials balances reflect the acquisition of subsidiaries inventories, which, due to the nature of their operations, are weighted towards holding higher volumes of raw material to enable cheese aging. Work in progress in FY20 of $11.6m (FY19: nil) predominantly relates to bulk cheese manufactured at Talbot Forest Cheese that is awaiting further manufacturing.

Finished goods inventory has increased to $186.5 million (FY19: $124.7 million). Tonnage of finished goods has increased to 32,109 MT (FY19: 23,318 MT). The increase relates to a larger holding of our core infant nutritional products and finished goods inventory held by Dairyworks and Talbot Forest Cheese.

Inventories were reviewed for impairment, resulting in a stock impairment provision totalling $2.0 million relating to finished goods ($1.8 million) and raw materials ($0.2 million) (FY19: $0.3 million all relating to finished goods). This increase primarily relates to production in late May which did not pass our stringent quality standards. Impaired finished goods were written down to net realisable value.

In addition, we have an onerous contracts provision of $0.3 million (FY19: $0.5 million); the reduction from prior year is due to product mix and a declining cost to manufacture.

Property, plant and equipment

Property, plant and equipment at $965.1 million, increased $119.9 million from FY19 at $845.2 million. The year-on-year increase is a consequence of total capital expenditure of $129.4 million, acquisitions through business combinations of $34.3 million, less depreciation of $40.0 million, impairment of $3.2 million, and net disposals of $0.6 million. The capital expenditure of $129.4 million primarily relates to our growth initiative projects with $93.9 million of total spend in FY20.

In February 2020, we commissioned our new North Island nutritional spray drier and related assets located in Pokeno. The construction of the nutritional spray dryer was budgeted to cost $258.3 million (excluding the cost of the land). Total spend on the project in FY20 was $64.1 million (FY19: $181.1 million, FY18: $12.7 million) for total spend to date of $257.9 million (excluding land).

During FY20 we also commissioned the capacity upgrade of our milk separation plant. Total spend in FY20 was $7.4 million (FY19: $6.5m) for total project spend of $13.9 million. In the year we also ramped up construction of our new dry storage facility. Total spend on the project in FY20 was $18.7 million (FY19: $0.9 million, FY18: $0.2 million) for total spend to date of $19.8 million.

Operational capital expenditure increased to $35.5 million from $18.5 million in FY19. The increase in expenditure was attributable to the upgrades at Talbot Forest Cheese ($4.7 million) and Dairyworks ($1.9 million), acquisition of replacement lactoferrin resin ($3.6 million), the fitout of the Christchurch office and upgrades to Dunsandel office building ($3.2 million), the upgrade of the Wetmix kitchen ($1.2 million), and Blended Steam Supply project ($1.2 million). The higher level of operational capital expenditure reflects the significant growth of the Group and its asset base over FY19 and FY20.

Acquisitions of Talbot Forest Cheese and Dairyworks

On 1 August 2019 the Group completed the purchase of Talbot Forest Cheese when Synlait Foods (Talbot Forest) Limited formally acquired Talbot Forest Cheese's Temuka assets and operations. Total consideration paid was $38.3 million. Brands of $1.7 million were acquired and $16.1 million of goodwill arose on acquisition.

On 1 April 2020 the Group completed the acquisition of 100% of the shares of Dairyworks for a purchase price of $112 million on a debt-free basis with the equity price being locked in with an effective date of 30 September 2019. After effective date adjustments for debt, working capital, and leakage – consideration of $63.6m was transferred to the vendors on 1 April 2020. Brands of $15.8 million were acquired and $43.4 million of goodwill arose on acquisition.

Trade and other payables

Trade and other payables at $238.8 million is up $22.8 million on last year's balance of $216.0 million. This variance is due to the trade and other payables balances of Dairyworks and Talbot Forest Cheese at 31 July 2020.

Contingent liability

The Group has included a contingent liability note in the annual financial statements relating to the Pokeno land covenant issue. There are a range of possible outcomes in this dispute meaning the Group is not able to reliably estimate a potential liability, if any. For further information please refer to the Contingent Liability note in the financial statements, page 125.

Total net debt

Total net debt (excluding lease liabilities) at year end, including both current and term debt facilities less cash on hand, was $527.0 million, an increase of $193.4 million over the FY19 balance of $333.6 million.

$ million	FY20	FY19
Current debt	$102.8	$99.6
Term debt (carry amount)	$426.8	$249.5
Transaction costs	$3.2	$0.5
Cash on hand	($5.9)	($16.0)
Total Net Debt (excluding lease liabilities)	**$527.0**	**$333.6**

Cash spent on investing activities of $225.0 million (FY19: $337.4 million) during the financial period, offset by cash from operating activities of $105.5 million (FY19: $136.6 million), resulted in a free cash outflow of $119.5 million from operating and investing activities. This together with cash outflows from interest and financing fees paid of $26.4 million (FY19: $18.1 million), repayment of lease liabilities $4.2m, and Dairyworks loans and borrowings of $43.2 acquired on acquisition account for the movement in net debt*. Operating cash flows are discussed further below.

With Net Debt* of $527.0 million, our gearing (Net Debt* / Net Debt* + Equity) is 46.5% (FY19: 40.4%) and our leverage (Net Debt* / EBITDA) is 3.08x (FY19: 2.19x).

* Net debt excluding lease liabilities

Derivatives

As at 31 July 2020 we held USD$525.5 million (net) in foreign exchange contracts as detailed in note 15 of the annual financial statements. These have been placed across a 24-month future period, in accordance with our Treasury Policy.

Given the recent appreciation in the NZD/USD exchange rate, we have mark to market unrealised gains associated with these contracts at year-end of $17.5 million after tax, a movement of $38.5 after tax year-on-year. As our foreign exchange contracts fully hedge against future USD receipts and payments, this unrealised gain is recognised in other reserves in equity rather than through the income statement. The impact of these foreign exchange contracts will play out in the periods in which they mature, and they will form part of our annual average NZD/USD exchange rate in those periods.

We also have in place a nominal balance of $57.3 million of interest rate swap agreements at year-end (FY19: $79.5 million) at various weighted average interest rates, generating an unrealised mark to market loss of $4.9 million after tax, a movement of $0.2m after tax year-on-year, with swap agreements unwinding partly offset by lower interest rates.

We continue to use dairy commodity derivatives to support the management of the risk of movement in dairy commodity prices. Dairy commodity derivatives with a nominal balance of NZD $12.0 million were in place at year end (FY19: NZD $5.3 million).

Year-on-year there was a $38.8 million movement in the cash flow hedge reserve from ($26.1) million in FY19 to $12.6 million in FY20. The cash flow hedge reserve relates to derivatives and the year-on-year movement is primarily explained by the movement in fair value of foreign exchange contacts as detailed above.

Operating cash flows

Operating cash flows at $105.5 million are down $30.9 million on FY19 ($136.6 million). The primary reason for this decrease was due to an unfavourable movement in working capital year-on-year with an increase in infant formula product on hand and additional working capital requirements of Dairyworks and Talbot Forest Cheese.

Funding facilities and covenants

At reporting date, the Group had in place four syndicated bank facilities with ANZ and BNZ:

1. Working Capital Facility – reviewed annually in September with a year-end facility limit of NZD $320.0 million. This is a dual currency (NZD & USD) facility.
2. Revolving Credit Facility A – maturing 1 August 2021 with a fixed facility limit of $150 million.
3. Revolving Credit Facility B – maturing 1 August 2023 with a fixed facility limit of $50 million.
4. Revolving Credit Facility C – maturing 1 August 2023 with a fixed facility limit of $50 million.

In addition to banking facilities, the company has on issue a $180.0m unsecured, subordinated, fixed rate bond maturing 17 December 2024.

Subsequent to reporting date, we have entered into an additional Revolving Credit Facility of $100m commencing 1 October 2020, stepping down to $70m on 1 January 2021 and maturing 1 May 2021. We have also reduced the working capital facility of $320m down to $250m and extended the revolving credit facility A to mature on 1 October 2021.

We have five bank covenants in place within our syndicated bank facility agreement. These are:

1. Interest cover ratio - EBITDA to interest expense of no less than 3.00x based on full year forecast result (FY20: 8.01x).
2. Minimum shareholders' funds – must exceed $295.5 million (FY20: $469.9 million).
3. Working capital ratio – must exceed 1.50x (FY20: 3.40x).
4. Leverage ratio – no more than 4.0x (FY20: 3.19x).
5. Senior leverage ratio - no more than 3.0x (FY20: 2.14x).

The company was compliant with our bank covenants at all times during the financial period.

Note that the covenants are calculated in accordance with our banking facilities agreement and include adjusting items that are not presented in the financial statements.

Angela Dixon
Chief Financial Officer

Synlait Pokeno, Waikato

FINANCIAL STATEMENTS

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DIRECTORS' RESPONSIBILITY STATEMENT

The Directors are pleased to present the financial statements for Synlait Milk Limited and its subsidiaries, Synlait Milk Finance Limited, The New Zealand Dairy Company Limited, Eighty Nine Richard Pearse Drive Limited, Synlait Business Consulting (Shanghai) Limited, Synlait Foods (Talbot Forest) Limited, Dairyworks Limited and Dairyworks (Australia) Pty Limited (together "the Group") as set out on pages 57 to 127 for the year ended 31 July 2020.

The Directors are responsible for ensuring that the financial statements present fairly the financial position of the Group as at 31 July 2020 and the financial performance and cash flows for the year ended on that date.

The Directors consider that the financial statements of the Group have been prepared using appropriate accounting policies, consistently applied and supported by reasonable judgements and estimates and that all relevant financial reporting and accounting standards have been followed.

The Directors believe that proper accounting records have been kept which enable, with reasonable accuracy, the determination of the financial position of the Group and facilitate compliance of the financial statements with the Financial Markets Conduct Act 2013.

For and on behalf of the Board.

Graeme Milne
Chair
25 September 2020

Willem Jan (Bill) Roest
Independent Director
25 September 2020

INCOME STATEMENT

For the year ended 31 July 2020

	Notes	2020 $'000	2019 $'000
Revenue	1	1,302,025	1,024,305
Cost of sales	2	(1,098,292)	(837,976)
Gross profit		**203,733**	**186,329**
Other income	1	404	898
Share of profit/(loss) from associates	19	33	(580)
Sales and distribution expenses	2	(32,318)	(26,836)
Administrative and operating expenses	2	(48,561)	(35,303)
Earnings before net finance costs and income tax		**123,291**	**124,508**
Finance expenses	10	(19,777)	(8,819)
Finance income	10	134	1,232
Loss on derecognition of financial assets	10,4	(1,747)	(1,842)
Net finance costs	10	**(21,390)**	**(9,429)**
Profit before income tax		**101,901**	115,079
Income tax expense	17	(26,693)	(32,840)
Net profit after tax for the period		**75,208**	**82,239**
Earnings per share			
Basic earnings per share (cents)	12	41.95	45.89
Diluted earnings per share (cents)	12	41.85	45.77

The accompanying notes form part of and are to be read in conjunction with these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 July 2020

	Notes	2020 $'000	2019 $'000
Profit for the period		75,208	82,239
Items that may be reclassified subsequently to profit and loss			
Effective portion of changes in fair value of cash flow hedges	15	53,882	(21,323)
Exchange differences on translation of foreign operations		(12)	-
Income tax on other comprehensive income	17	(15,087)	5,971
Total items that may be reclassified subsequently to profit and loss		38,783	(15,352)
Other comprehensive income for the year, net of tax		38,783	(15,352)
Total comprehensive income for the year		113,991	66,887

The accompanying notes form part of and are to be read in conjunction with these financial statements.

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 July 2020

Group	Notes	Share Capital $'000	Employee Benefits Reserve $'000	Cash Flow Hedge Reserve $'000	Foreign Currency Translation Reserve $'000	Retained Earnings $'000	Total Equity $'000
Equity as at 1 August 2018		268,074	930	(10,796)	-	166,536	424,744
Profit or loss for the year		-	-	-	-	82,239	82,239
Other comprehensive income							
Effective portion of changes in fair value of cash flow hedges		-	-	(21,410)	-	-	(21,410)
Movement in time value hedge reserve		-	-	87	-	-	87
Income tax on other comprehensive income		-	-	5,971	-	-	5,971
Total other comprehensive income		-	-	(15,352)	-	-	(15,352)
Employee benefits reserve	13,14,17	-	728	-	-	-	728
Total contributions by and distributions to owners		-	728	-	-	-	728
Equity as at 31 July 2019		268,074	1,658	(26,148)	-	248,775	492,359
Profit or loss for the year		-	-	-	-	75,208	75,208
Other comprehensive income							
Effective portion of changes in fair value of cash flow hedges		-	-	53,882	-	-	53,882
Exchange differences on translation of foreign operations		-	-	-	(12)	-	(12)
Income tax on other comprehensive income		-	-	(15,087)	-	-	(15,087)
Total other comprehensive income		-	-	38,795	(12)	-	38,783
Employee benefits reserve	13,14,17	470	(336)	-	-	-	134
Total contributions by and distributions to owners		470	(336)	-	-	-	134
Equity as at 31 July 2020		268,544	1,322	12,647	(12)	323,983	606,484

The accompanying notes form part of and are to be read in conjunction with these financial statements.

STATEMENT OF FINANCIAL POSITION

As at 31 July 2020

	Notes	2020 $'000	2019 $'000 (restated)
ASSETS			
Current assets			
Cash and cash equivalents		5,887	16,007
Trade and other receivables	4	63,057	61,933
Intangible assets	8	4,230	3,686
Goods and services tax refundable		6,398	3,689
Income accruals and prepayments		12,404	9,554
Inventories	5	269,384	164,849
Derivative financial instruments	15,16	22,530	2,358
Other current assets		2,500	20,500
Total current assets		**386,390**	**282,576**
Non-current assets			
Property, plant and equipment	7	965,104	845,202
Intangible assets	8	42,503	16,428
Goodwill	8,18	65,545	6,026
Other investments	19	143	110
Derivative financial instruments	15,16	14,084	45
Right-of-use assets	9	18,497	-
Total non-current assets		**1,105,876**	**867,811**
Total assets		**1,492,266**	**1,150,387**
LIABILITIES			
Current liabilities			
Loans and borrowings	11	102,837	99,626
Trade and other payables	6	238,770	216,020
Current tax liabilities		24,561	29,220
Derivative financial instruments	15,16	14,148	27,960
Lease liabilities	9	4,422	-
Total current liabilities		**384,738**	**372,826**
Non-current liabilities			
Loans and borrowings	11	426,754	249,482
Deferred tax liabilities	17	54,647	25,034
Derivative financial instruments	15,16	4,805	10,686
Lease liabilities	9	14,838	-
Total non-current liabilities		**501,044**	**285,202**
Total liabilities		**885,782**	**658,028**
Equity			
Share capital	12	268,544	268,074
Reserves	14	13,957	(24,490)
Retained earnings	14	323,983	248,775
Total equity attributable to equity holders of the Group		**606,484**	**492,359**
Total liabilities and equity		**1,492,266**	**1,150,387**

Comparative numbers for goodwill and deferred tax have been restated due to a prior period error. Refer to Note 18 for further detail.

The accompanying notes form part of and are to be read in conjunction with these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 31 July 2020

	Notes	2020 $'000	2019 $'000
Cash flows from operating activities			
Cash receipts from customers		1,316,076	1,025,168
Cash paid for milk purchased		(545,792)	(461,369)
Cash paid to other creditors and employees		(635,402)	(403,420)
Net movement in goods and services tax		(2,709)	2,846
Income tax payments		(26,633)	(26,670)
Net cash inflow from operating activities	3	**105,540**	**136,555**
Cash flows from investing activities			
Acquisition of subsidiaries, net of cash acquired	18	(72,927)	(18,000)
Interest received		134	1,232
Purchase of property, plant and equipment		(139,212)	(309,314)
Proceeds from sale of property, plant and equipment		242	(147)
Purchase of intangible assets		(13,262)	(11,127)
Net cash outflow from investing activities		**(225,025)**	**(337,356)**
Cash flows from financing activities			
Proceeds from the issuance of subordinated bonds	11	180,000	-
Transaction costs paid on issue of subordinated bonds		(3,370)	-
(Repayment)/drawdown of borrowings	18	(43,224)	152,300
Net movement in working capital facility		3,211	50,305
Interest paid		(23,048)	(18,069)
Repayment of lease liabilities		(4,185)	-
Net cash inflow from financing activities		**109,384**	**184,536**
Net decrease in cash and cash equivalents		**(10,101)**	**(16,265)**
Cash and cash equivalents at the beginning of the financial year		16,007	32,129
Effects of exchange rate changes on cash and cash equivalents		(19)	143
Cash and cash equivalents at end of year		**5,887**	**16,007**

The accompanying notes form part of and are to be read in conjunction with these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

REPORTING ENTITY

The consolidated financial statements ("financial statements") presented are those of the Group, including Synlait Milk Limited and its subsidiaries Synlait Milk Finance Limited, The New Zealand Dairy Company Limited, Eighty Nine Richard Pearse Drive Limited, Synlait Business Consulting (Shanghai) Limited, Synlait Foods (Talbot Forest) Limited, Dairyworks Limited and Dairyworks (Australia) Pty Limited.

Synlait Milk Limited is primarily involved in the manufacture and sale of dairy products.

The parent company, Synlait Milk Limited, is a profit oriented entity, domiciled in New Zealand, registered under the Companies Act 1993 and listed on the New Zealand Stock Exchange and the Australian Securities Exchange. Synlait Milk Limited is a FMC reporting entity under the Financial Market Conducts Act 2013 and its financial statements comply with that Act.

BASIS OF PREPARATION

The financial statements of the Group have been prepared in accordance with Generally Accepted Accounting Practice. They comply with New Zealand equivalents to International Financial Reporting Standards ('NZ IFRS') and other applicable Financial Reporting Standards, as applicable for profit oriented entities. The consolidated financial statements also comply with International Financial Reporting Standards ('IFRS').

Certain comparative figures have been reclassified during the year for consistency with the current year presentation. These classifications had no effect on the reported results of operations.

The financial statements were authorised for issue by the directors on 25 September 2020.

Basis of measurement

These financial statements have been prepared on the historical cost basis except for certain items as identified in specific accounting policies.

Functional and presentation currency

Items included in the financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The financial statements are presented in New Zealand Dollars ($), which is the Company's functional currency and are rounded to the nearest thousand ($000).

Transactions and balances

Transactions in foreign currencies are translated to the functional currency at the exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date.

Use of accounting estimates and judgements

The preparation of these financial statements in conformity with NZ IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates and assumptions.

Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Key sources of estimation uncertainty and key judgements relate to derecognition of financial assets, the assessment of impairment of inventory and property plant and equipment, and the identification and valuation of goodwill and any other indefinite life intangible assets. The individual notes in the financial statements provide additional information.

COVID-19

In March 2020, the World Health Organisation declared the outbreak of COVID-19 as a pandemic. The Group's operations were deemed an essential service and therefore continued throughout the various New Zealand Government COVID-19 alert levels. The Group's primary focus in responding to the pandemic has been to protect the safety of its staff and to implement appropriate controls around its production facilities. Access restrictions were put in place at all facilities, including staff working from home where possible, additional cleaning and security provisions were also put in place on site and other social distancing measures were adopted.

The COVID-19 pandemic has resulted in an increase in uncertainty in both global and local markets. Management assessed the impact of COVID-19 on all aspects of the balance sheet, in particular the carrying value of receivables and inventory, impairment of assets such as goodwill, and any impact from currency volatility during this period on the Group's portfolio of derivatives. Management has determined that there has been a modest impact on the balance sheet and the performance of the Group in FY20.

The Group has continued to assess the impact of any changes to New Zealand Government COVID-19 alert levels which have occurred subsequent to balance date and up to the date of the approval of the financial statements. The Group has considered the impact of these changes and they are not expected to have a material impact on either the Group's operations or its financial statements.

BASIS OF CONSOLIDATION

The Group's financial statements consolidate the financial statements of Synlait Milk Limited and its subsidiaries, accounted for using the acquisition method, and the results of its associates, accounted for using the equity method. Intercompany transactions and balances between group companies are eliminated upon consolidation.

SIGNIFICANT ACCOUNTING POLICIES

Accounting policies, accounting estimates and judgements that summarise the measurement basis used and are relevant to the understanding of the financial statements are provided throughout the accompanying notes and are designated by a shaded area.

The accounting policies adopted have been applied consistently throughout the periods presented in these financial statements, except for the change in accounting policy relating to the adoption of NZ IFRS 16.

Standards, amendments and interpretations to existing standards that are not yet effective

There are no standards that are not yet effective and expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

Changes in accounting policies

During the period the Group adopted the following new standards;

NZ IFRS 16 'Leases' (effective 1 August 2019)

Effective 1 August 2019, the Group has adopted NZ IFRS 16, which supersedes NZ IAS 17 Leases (NZ IAS 17) and related interpretations. Under NZ IAS 17, leases were previously classified as either operating or financing for lessees based on an assessment of whether the lease transferred significantly all of the risks and rewards incidental to ownership of the underlying asset to the Group. As the Group's leases were previously classified as operating, straight-line operating lease expense was recognised over the lease term in the comparative period.

NZ IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees, with a right-of-use asset ("ROU asset") representing the Group's right to use the underlying asset, and a lease obligation representing its obligation to make lease payments. Amortisation expense for ROU assets and interest expense for lease obligations replaces the straight-line operating lease expense recognised under NZ IAS 17.

The Group has applied NZ IFRS 16 using the modified retrospective approach, under which the initial ROU asset is measured at an amount equal to the lease liability resulting in no impact to retained earnings at 1 August 2019. Short-term and low-value recognition exemptions were applied, as well as practical expedients allowing for the use of hindsight to assess the lease term for contracts with extension options and the exclusion of leases with a term of less than one year remaining at the transition date. The Group also utilised the practical expedient which allowed for all existing contracts which were previously identified as leases to be treated as leases under NZ IFRS 16. NZ IFRS 16 was not applied to contracts which were not previously treated as leases under NZ IAS 17 as at transition date.

The impact of transition is outlined under Note 9, with changes in accounting policies outlined below:

Lease definition

At inception of a contract, the Group assesses whether the contract is, or contains, a lease. A contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. An identified asset may be implicitly or explicitly specified in a contract, but must be physically distinct, and must not have the ability for substitution by a lessor. The Company has the right to control an identified asset if it obtains substantially all of its economic benefits and either pre-determines, or directs how and for what purpose the asset is used.

Measurement of right-of-use assets and lease obligations

On initial application, the Group elected to record ROU assets equal to the corresponding present value of the remaining lease liability. Subsequent additions were measured at the initial amount of the lease obligation adjusted for any lease payments made at, or before, the commencement date, plus any initial direct costs incurred, less any lease incentives received.

The ROU asset is subsequently depreciated on a straight-line basis over the shorter of the term of the lease, or the useful life of the asset determined on the same basis as the Group's property, plant and equipment. The ROU asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease obligation.

The lease obligation is initially measured at the present value of lease payments remaining at the lease commencement date, discounted using the Group's incremental borrowing rate. Lease payments included in the measurement of the lease obligation, when applicable, may comprise fixed payments, variable payments that depend on an index or rate, amounts expected to be payable under a residual value guarantee and the exercise price under a purchase, extension or termination option that the Group is reasonably certain to exercise.

The lease obligation is subsequently measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee, or if the Group changes its assessment of whether it will exercise a purchase, extension or termination option. When the lease obligation is remeasured, a corresponding adjustment is made to the carrying amount of the ROU asset.

Recognition exemptions

The Group has elected not to recognise ROU assets and lease obligations for short-term leases that have a lease term of twelve months or less or for leases of low-value assets. Payments associated with these leases are recognised as an operating expense on a straight-line basis over the lease term within costs and expenses in the consolidated Income Statement. The Group has also elected to apply a single discount rate to portfolios of leases with reasonably similar characteristics.

PERFORMANCE

This section covers the Group's financial performance and includes the following notes:

01. REVENUE RECOGNITION AND SEGMENT INFORMATION

Sales of goods

The Group manufactures and sells a range of milk powder, milk powder related products, liquid milk, cheese and butter to customers. Revenue from contracts with customers is recognised when the control of the goods has been transferred to customers, being at the point when the goods are delivered. Delivery of goods is completed (i.e. the performance obligation is fulfilled) when the goods have been delivered pursuant to the terms of the specific contract agreed with the customer and the risks associated with ownership have been transferred to the customer.

Revenue is measured according to the contracted price agreed with customers, which represents fair value of the consideration received or receivable, net of returns, discounts and allowances. Revenue is only recognised to the extent that it is highly probable that a significant reversal will not occur. The payment terms vary depending on the individual contracts. No deemed financing components are present as there are no significant timing differences between the payment terms and revenue recognition.

	2020 $'000	2019 $'000
Dairy products	1,302,025	1,024,305
Other sundry income	404	898
Total income	**1,302,429**	**1,025,203**

Description of segments

The Group operates in one industry, being the manufacture and sale of milk powder, milk powder related products, liquid milk, cheese and butter. The Board makes resource allocation decisions based on expected cash flows and results of the Group's operations as a whole and the Group therefore has one segment.

As a result of the recent acquisitions of both Synlait Foods (Talbot Forest) Limited and Dairyworks Limited, Management is currently reviewing the way in which it internally reports on the business activities of the Group and this may result in changes to how activities are reported to the Chief Operating Decision Maker in the future. Any changes made may have a corresponding impact on segment results reported in the financial statements.

Revenues of approximately 64% (2019: 66%) are derived from the top three external customers. The proportion of sales revenue by geographical area is summarised below:

	2020	2019
China*	5%	8%
Rest of Asia	19%	24%
Middle East and Africa	8%	7%
New Zealand	43%	34%
Australia	22%	24%
Rest of World	3%	3%
Total	100%	100%

* The Group operates in one principal geographical area being New Zealand. Although the Group sells to many different countries, it is understood that a significant proportion of both infant nutritional and ingredients sales are ultimately consumed in China.

02. EXPENSES

	2020 $'000	2019 $'000
The following items of expenditure are included in cost of sales		
Depreciation and amortisation	38,851	24,289
Employee benefit expense	78,748	48,711
KiwiSaver contributions	1,656	1,166
Export freight	11,104	9,524
Rent and storage	2,471	874
Increase/(decrease) in inventory provision	1,702	(1,805)
Decrease in onerous contract provision	(156)	(809)
The following items of expenditure are included in sales and distribution		
Depreciation and amortisation	5,936	1,625
Employee benefit expense	13,137	10,195
KiwiSaver contributions	376	252
Rent and storage	1,284	3,637
The following items of expenditure are included in administrative and operating		
Depreciation and amortisation	3,273	1,725
Employee benefit expense	21,467	17,986
KiwiSaver contributions	618	480
Information services	5,118	3,502
Directors fees	802	752
Share based payments expense	523	644
Impairment of intangible assets	1,561	123
Consultancy	3,268	2,768
Strategic Initiatives	1,362	162
Deloitte services included in administrative and operating expenses		
Statutory audit fee	276	185
Half year accounts review	57	45
Other assurance services	130	77
Taxation compliance	53	69
	516	376

The year on year increase in some expenditure categories is in part due to the acquisition of Dairyworks Limited and Synlait Foods (Talbot Forest) Limited. These two subsidiaries contributed $1.4m to sales and distribution expenditure and $3.7m to administrative and operating expenditure since 1 August 2019. Refer to Note 18 for further detail on both acquisitions.

03. RECONCILIATION OF PROFIT AFTER INCOME TAX TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	2020 $'000	2019 $'000
Profit for the year	75,208	82,239
Non-cash and non-operating items		
Depreciation and amortisation of non-current assets	43,112	27,639
Depreciation of right-of-use assets	4,948	-
Loss on sale of property, plant and equipment	355	147
Impairment of property, plant and equipment and intangible assets	4,761	123
Impairment recovery on property, plant and equipment	(2,958)	-
Share of (gain)/loss from associate	(33)	580
Non-cash share based payments expense	523	644
Interest costs classified as financing cash flow	19,777	8,819
Interest received classified as investing cash flow	(134)	(1,232)
Loss on derecognition of financial assets	1,747	1,842
Deferred tax	9,291	4,341
(Gain)/loss on derivative financial instruments	(23)	22
Unrealised foreign exchange losses/(gains)	6	(143)
Movements in working capital		
Decrease/(increase) in trade and other receivables	1,833	(14,788)
(Increase) in prepayments	(2,850)	(5,214)
(Increase) in inventories	(104,533)	(19,444)
(Increase)/decrease in goods and services tax refundable	(2,709)	2,846
Increase in trade and other payables	34,673	46,306
(Decrease)/increase in current tax liabilities	(4,659)	1,828
Working capital items acquired	27,205	-
Net cash inflow from operating activities	**105,540**	**136,555**

WORKING CAPITAL

The working capital section gives information about the short term assets and liabilities of the Group. This section includes the following notes:

04. TRADE AND OTHER RECEIVABLES

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less they are classified as current assets. If not, they are classified as non-current assets.

Impairment

The Group recognises a loss allowance for expected credit losses (“ECL”) on trade and other receivables. The Group measures the provision for ECL using the simplified approach to measuring ECL which uses a lifetime expected loss allowance for all trade receivables. The Group’s credit loss model requires the Group to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition of the financial assets. Therefore, it is no longer necessary for a credit event to have occurred before credit losses are recognised.

The model is based on the Group’s historical credit loss experience, adjusted for factors that are specific to the debtors, general economic conditions and an assessment of both the current as well as the forecast direction of conditions at the reporting date.

Lifetime ECL represents the expected credit losses that will result from all possible default events over the expected life of a financial instrument. The expected credit loss is estimated as the difference between all contractual cash flows that are due to the Group in accordance with the contract and all the cash flows that the Group expects to receive, discounted at the original effective interest rate.

The Group writes off a financial asset when there is information indicating that the debtor is in such severe financial difficulty and there is no reasonable and realistic prospect of recovery.

Furthermore, other impairment losses on an individual basis are determined by an evaluation of the exposures on an instrument by instrument basis. All individual instruments that are considered significant are subject to this approach.

Credit Risk Management

The Group activities expose it to credit risk which refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Group. Trade and other receivables are potentially subject to credit risk. The Group performs credit evaluations on trade customers. The Group continuously monitors the credit quality of its major receivables and does not anticipate non-performance of those customers, nor has there been historical non-performance of these customers. The Group also maintains strict controls for any credit reviews such as credit increases.

The receivables assignment processes ensure that the Group’s trade receivables are materially managed in an efficient and effective basis.

The carrying amount of financial assets recorded in the financial statements represents the Group’s maximum exposure to credit risk.

Included in trade receivables are debtors which are past due at balance date, as payment was not received within 30 days, and for which no provision has been made as there has not been a significant change in credit quality and the amounts are still considered fully recoverable. No collateral is held over these balances and trade credit insurance cover was not obtained in respect of these receivables. Interest is not charged on overdue debtors.

In the past six financial years, the Group has not written off any bad debts, although it has recognised provisions for debts when collection was considered doubtful. The historical analysis of bad debts on a customer basis assists in the determination of any increases in credit risk since initial recognition. There are no significant credit risk concentrations as at 31 July 2020. Three customers represent 70% of the overdue receivables. There were no other forward looking indicators to indicate increases in credit risk. Refer to the basis of preparation section of the accounts for further detail on the impact of COVID-19 on receivables.

For cash and cash equivalents the Group has determined that all bank balances have low credit risk at each reporting period as they are held by reputable international banking institutions.

The Group has not changed its overall strategy regarding the management of risk from 2019.

	2020 $'000	2019 $'000
Trade receivables	56,484	58,076
Provision for doubtful and impaired receivables	(977)	(395)
Net trade receivables	**55,507**	**57,681**
Other receivables	7,550	4,252
Total receivables	**63,057**	**61,933**

04. TRADE AND OTHER RECEIVABLES (CONTINUED)

(a) Impaired receivables

As at 31 July 2020, trade receivables of $9.2m were overdue (2019: $7.1m). These relate to a number of independent customers for whom there is no recent history of default. The majority has since been collected but $3.9m remains unpaid which is expected to be collected in the 2021 financial year. The aging analysis of these overdue trade receivables is as follows:

	2020 $'000	2019 $'000
Overdue by		
0 to 30 days	5,950	6,021
30 to 60 days	549	60
Over 60 days	2,725	1,044
Total overdue trade receivables	9,224	7,125

(b) Allowance for bad and doubtful receivables

The Group has recognised a loss of $0.4m in relation to unrecoverable trade receivables during the year (2019: $0.3m). This relates to debtors that are overdue by more than 60 days. The Group has also recognised a loss of $0.1m for estimated receivables impairment under NZ IFRS 9 Financial Instruments (2019: $0.1m).

(c) Trade and other receivables

Accounts receivable are amounts incurred in the normal course of business.

Receivables denominated in currencies other than the functional currency comprise NZ$38.5m (2019: $52.6m) of USD and AUD denominated trade receivables.

(d) Derecognised financial assets

The Group has derecognised trade receivables that have been sold to two banks under the terms of receivables purchase agreements entered into during January 2015 and January 2016. The Group routinely assess the terms of the agreements and has determined that substantially all the risks and rewards have been transferred to the banks. Receivables selected for assignment are with customers with strong credit ratings and good payment histories. This minimises the risk (and therefore consequences) of late payment or default, as well as resulting in little volatility in the present value of future cash flows in relation to assigned receivables under the various scenarios detailed in the terms of the two agreements. An evaluation of external evidence of credit risk has also been performed for each customer. The Group has assigned $131.3m of receivables as at 31 July 2020 (2019: $109.0m).

The Group has assessed its continuing involvement in the assigned receivables and determined that the fair value of continuing involvement is immaterial. The Group reassesses the facility for qualification for derecognition at each reporting date, when the terms of the facility are amended, and assesses each new customer at the initial assignment of a receivable. No new customers were assigned during the period.

If the Group's customers defaulted on all trade receivables that have been derecognised at balance date, the Group would be required to pay a late payment charge of $5,351 per day (2019: $9,003) for each day that these receivables remain overdue, assuming that market conditions remain unchanged from reporting date. The likelihood that debtors will fall overdue or remain overdue for a long period of time is small, given the strong credit ratings and good payment histories of the customers whose receivables have been selected for assignment.

The loss for the period of $1.7m (2019: $1.8m) arising from derecognition of assigned receivables is the discount paid to the banks for acquiring these receivables.

05. INVENTORIES

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and where applicable, direct labour and an appropriate proportion of variable and fixed overhead expenditure, the latter being allocated on the basis of normal operating capacity. Cost is determined on a weighted average basis and in the case of manufactured goods, includes direct materials, labour and production overheads. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Present obligations arising under onerous contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Group has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Key management judgement is applied in assessing inventory impairment, and therefore net realisable value of inventory. Impairment is tested in three ways, stock provision, onerous contracts provision, and inventory impairment. The stock provision considers the condition of inventory and therefore requires a high level of management judgement, whereas the onerous contracts and impairment calculations are largely formulaic.

The stock provision tests for the physical impairment of both raw materials and finished goods. Physical impairment can be for a variety of reasons, including damage, expiry, or obsolescence. Management judgement is required as often indicators of impairment can be removed through further investigation or rework meaning that no write-down to net realisable value is required. Management consider historical rework process results and future rework plans in making that judgement.

Estimates are required in relation to net realisable value, which is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. Net realisable value is determined by reference to historic achieved market prices, future contracted sales and global dairy trade auction results. Reviewing the net realisable values is carried out by management on a monthly basis, using their judgement in determining expected future proceeds based on current indicators of the condition of inventory.

A key management estimation in determining inventory cost is the Monthly Milk Price which is derived from a forecast milk price for the year. The Monthly Milk Price forms a key component of the product cost through the year.

	2020	2019
	$'000	$'000
Raw materials at cost	71,305	40,058
Work in progress at cost	11,573	-
Finished goods at cost	178,336	118,090
Finished goods at net realisable value	8,170	6,701
Total inventories	**269,384**	**164,849**

Raw material inventories at $71.3m (13,614 MT) have increased (2019: $40.1m, 11,307 MT), primarily due to the acquisitions of subsidiaries. The tonnage has increased at a slower rate than the value as Synlait Milk Limited holds less raw materials by volume but comparatively more high-value infant additives.

Finished goods have increased to $186.5m (32,109 MT) (2019: $124.8m, 23,318 MT). The increase relates to inventory held by subsidiaries and an increased holding of our core infant formula products. Finished goods held at net realisable value have increased as a result of our acquisitions of subsidiaries.

The cost of inventories recognised as an expense during the year was $1,098.3m (2019: $838.0m). The cost of inventories recognised as an expense includes $10.9m (2019: $7.4m) in respect of write downs of inventory to net realisable value.

The total inventory provision as at reporting date was $2.0m, of which $1.8m related to finished goods and $0.2m to raw materials (2019: $0.3m, all related to finished goods). The increase primarily relates to production in late May which did not pass our stringent quality standards.

In addition, the total onerous contracts provision as at reporting date was $0.3m (2019: $0.5m).

06. TRADE AND OTHER PAYABLES

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less otherwise they are presented as non-current liabilities.

Trade and other payables are recognised initially at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method. Payables that are settled within a short duration are not discounted.

	2020	2019
	$'000	$'000
Trade payables	106,942	82,122
Accrued expenses	118,853	126,690
Employee entitlements	12,809	7,208
Other payables	166	-
Total trade and other payables	**238,770**	**216,020**

Payables denominated in currencies other than the functional currency comprise NZ$11.9m (2019: $0.5m) of USD, EUR and AUD denominated trade payables and accruals.

LONG TERM ASSETS

The assets section provides information about the long term investments made by the Group to operate the business and generate returns to shareholders. This section includes the following notes:

07. PROPERTY, PLANT AND EQUIPMENT

Recognition and measurement

Property, plant and equipment are initially measured at cost less accumulated depreciation.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located.

When a self-constructed asset meets the definition of a qualifying asset under NZ IAS 23 Borrowing Costs, borrowing costs directly attributable to the construction of the asset are capitalised until such a time as the asset is substantially ready for its intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

When major components of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

Depreciation

Depreciation of property, plant and equipment is recognised in profit or loss on a straight line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated.

Capital work in progress is not depreciated. The total cost of this work is transferred to the relevant asset category on the completion of the project and then depreciated.

Estimation and judgement is also required in the selection and application of useful lives. It is management's best estimate that the useful lives adopted adequately reflect the flow of resources and the economic benefits required and derived in the use and servicing of property, plant, and equipment.

The estimated useful lives for the current and comparative periods are as follows:

Buildings	**10 - 50 years**
Plant and equipment	**3 - 35 years**
Fixtures and fittings	**2 - 25 years**

Depreciation methods, useful lives and residual values are reassessed at each reporting date.

07. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

Impairment

Estimation and judgement is required in the impairment of property, plant, and equipment. The Group estimates or exercises judgement in assessing indicators of impairment, forecasting future cash flows and determining other key assumptions used for assessing fair values (less costs of disposal) or value in use.

	Land $'000	Buildings $'000	Plant and Equipment $'000	Fixtures and Fittings $'000	Capital Work in Progress $'000	Total $'000
Cost						
Balance as at 1 August 2018	7,457	136,711	419,849	9,557	80,675	654,249
Additions	27,500	-	-	-	306,100	333,600
Reclassification/transfer	-	46,457	95,610	4,499	(146,566)	-
Disposals	-	(127)	(2,251)	(1,283)	-	(3,661)
Balance as at 31 July 2019	34,957	183,041	513,208	12,773	240,209	984,188
Additions	-	-	-	-	129,381	129,381
Additions through business combinations (note 18)	1,350	4,610	26,060	2,021	233	34,274
Reclassification/transfer	458	103,202	185,441	11,213	(300,314)	-
Impairment	-	-	(1,050)	-	(2,301)	(3,351)
Disposals	-	(75)	(2,777)	(746)	-	(3,598)
Balance as at 31 July 2020	36,765	290,776	720,882	25,262	67,208	1,140,893
Accumulated depreciation						
Balance as at 1 August 2018	-	18,360	92,847	5,373	-	116,580
Depreciation (note 2)	-	4,236	20,060	1,403	-	25,699
Disposals	-	(44)	(1,964)	(1,283)	-	(3,291)
Balance as at 31 July 2019	-	22,552	110,943	5,493	-	138,988
Depreciation (note 2)	-	6,909	29,869	3,177	-	39,955
Impairment	-	-	(151)	-	-	(151)
Disposals	-	(33)	(2,300)	(668)	-	(3,001)
Balance as at 31 July 2020	-	29,426	138,363	8,000	-	175,789
Carrying amounts						
As at 31 July 2019	34,957	160,489	402,265	7,282	240,209	845,202
As at 31 July 2020	36,765	261,350	582,521	17,260	67,208	965,104

(a) Impairment

During the period, property, plant, and equipment have been examined for impairment. A $3.2m (2019: $nil) impairment charge has been recognised to reflect the write-down of select assets to the higher of their fair value less costs of disposal (FVLCOD) and value-in-use. Of the $3.2m impairment charge, $3.0m related to the write-down of blending and canning over-cap equipment determined to not be fit for purpose due to engineering and design deficiencies and $0.2m related to other projects which were assessed as being unlikely to provide future economic benefit. Compensation for impairment of $3.0m has been recognised in profit and loss on the basis that the Group is contractually entitled to compensation relating to the write-down of the blending and canning over-cap equipment which was determined to not be fit for purpose. FVLCOD and value-in-use was determined to be $nil for all assets determined to be impaired.

(b) Capital work in progress

Assets under construction includes capital expenditure projects, until they are commissioned and transferred to property, plant and equipment. Capital work in progress of $67.2m is significantly lower than 2019 ($240.2m) due to the completion of Synlait Pokeno and resulting transfer from work in progress to fixed assets.

(c) Capitalised borrowing costs

During the year, the Group has capitalised borrowing costs amounting to $2.1m (2019: $7.5m) on qualifying assets. Interest has been capitalised at the rate at which borrowing has been specifically drawn to fund the qualifying asset. In the year, borrowing costs were capitalised for Synlait Pokeno and the Dry Store 4, enterprise resource planning system, and separator capacity upgrade projects. Borrowing costs continue to be capitalised for the Dry Store 4 and enterprise resource planning system upgrade projects.

08. INTANGIBLE ASSETS

Goodwill

Goodwill arises on the acquisition of subsidiaries and represents the excess of the cost of the acquisition over the net of the fair values of the assets and liabilities of the subsidiaries acquired. Goodwill is tested for impairment annually and is carried at cost as established at the date of acquisition of the subsidiary, less accumulated impairment losses, if any.

For the purposes of impairment testing, goodwill is allocated to cash-generating units (CGU) that are expected to benefit from the business combination in which the goodwill arose. The recoverable amount of CGUs is the higher of fair value less costs to sell and value in use. If this recoverable amount is less than the carrying amount of the CGU an impairment loss is recognised immediately in the profit and loss, and it is not subsequently reversed.

Brands

Purchased brands have been assessed as indefinite life intangible assets, after considering factors such as the expected use of the assets, the period of legal control, the typical product life cycle of these assets, the industry in which the assets are operating, and the level of maintenance expenditure required. Purchased brands are initially recognised at fair value if acquired as part of a business combination, and are tested for impairment annually, or more frequently if there are any indicators of impairment, on the same basis as goodwill.

Patents, trademarks and other rights

Separately acquired patents and trademarks are shown at historical cost. Patents and trademarks have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight line method to allocate the cost of patents and trademarks over their estimated useful lives of 10 years.

Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on a straight line basis over their estimated useful lives of 3 to 10 years.

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Group are recognised as intangible assets.

New Zealand Units (NZU)

New Zealand Units are purchased to offset carbon emissions under the New Zealand Emissions Trading Scheme. The units are measured at cost.

Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment.

An impairment loss is recognised if the carrying amount of an asset or its CGU exceeds its recoverable amount. A CGU is the smallest identifiable asset group that generates cash flows that are largely independent from other assets and groups.

Impairment losses recognised in respect of CGU's are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of any other assets in the unit (or group of units) on a pro rata basis.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses are recognised in profit or loss.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss has been recognised. An impairment loss in relation to goodwill is not reversed.

08. INTANGIBLE ASSETS (CONTINUED)

	Goodwill	Brands	Patents, Trademarks and Other Intangibles	Computer Software	Intangibles in Progress	New Zealand Units	Total
	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Year ended 31 July 2019							
Opening net book amount (restated)	6,026	-	352	4,532	3,200	2,967	17,077
Additions	-	-	497	3,170	7,117	5,765	16,549
Development costs recognised as an asset	-	-	-	-	(3,667)	-	(3,667)
Amortisation charge (note 2)	-	-	(131)	(1,809)	-	-	(1,940)
Asset disposals/surrendered	-	-	-	-	(123)	(1,756)	(1,879)
Closing net book value (restated)	**6,026**	-	**718**	**5,893**	**6,527**	**6,976**	**26,140**
Year ended 31 July 2019							
Current	-	-	-	-	-	3,686	3,686
Non-current	6,026	-	718	5,893	6,527	3,290	22,454
Closing net book value (restated)	**6,026**	-	**718**	**5,893**	**6,527**	**6,976**	**26,140**
Year ended 31 July 2020							
Opening net book value	6,026	-	718	5,893	6,527	6,976	26,140
Additions	-	-	908	5,234	11,328	4,138	21,608
Acquisition through business combination (note 18)	59,519	17,545	107	263	160	-	77,594
Development costs recognised as an asset	-	-	25	15	(6,183)	-	(6,143)
Impairment (note 2)	-	-	-	-	(1,561)	-	(1,561)
Amortisation charge (note 2)	-	-	(344)	(2,813)	-	-	(3,157)
Asset disposals/surrendered	-	-	-	-	-	(2,203)	(2,203)
Closing net book value	**65,545**	**17,545**	**1,414**	**8,592**	**10,271**	**8,911**	**112,278**
Year ended 31 July 2020							
Current	-	-	-	-	-	4,230	4,230
Non-current	65,545	17,545	1,414	8,592	10,271	4,681	108,048
Closing net book value	**65,545**	**17,545**	**1,414**	**8,592**	**10,271**	**8,911**	**112,278**

Intangibles in progress of $10.3m at balance date is predominantly constituted of project to date spend on systems and process development.

The opening goodwill balance for the year ended 31 July 2019 has been restated to correct an immaterial prior period error which was identified during the current year. Please refer to Note 18 for further detail.

(a) Impairment tests for indefinite life intangibles

As at 31 July 2020 management has determined that there is no impairment of any CGU containing goodwill.

For the purposes of goodwill impairment testing, goodwill has been allocated to two CGU groups; the Auckland blending and canning CGU and consumer foods CGU. The recoverable amounts of the CGU's have been determined based on value in use.

The value-in-use calculation uses five year future cash flows based on Board approved business plans, due diligence performed as part of the acquisition, and managements past experience. Based on projected future cash flows, management has determined that the recoverable amount of the CGU's exceeds the combined carrying values and therefore goodwill is not impaired. The business plans were modelled using the following key assumptions:

	2020	2019
Annual revenue growth rates	(0.6%) - 7.9%	0.0%
Allowance for increase in expenses	1.9% - 4.0%	2.5%
Pre-tax discount rate	10.7% - 15.2%	11.8%
Terminal growth rate	0.0% - 2.0%	0.0%

Indefinite life intangibles, which is comprised entirely of brands, has been calculated using the relief from royalty method. The impairment testing was modelled using the following key assumptions:

	2020	2019
Annual revenue growth rates	(30.0%)* - 7.9%	0.0%
Allowance for increase in expenses	1.9% - 4.0%	2.5%
Royalty rate	25.0%	0.0%
Post-tax discount rate	8.5% - 11.2%	8.5%
Terminal growth rate	0.0% - 2.0%	0.0%

*This range includes a 30% decrease in Talbot Forest branded FY21 sales, reflecting a conservative downside resulting from the recent voluntary recall of Talbot Forest branded cheese from customers throughout New Zealand. Refer to Note 18 for further information on the brand assets acquired.

Management has carried out a sensitivity analysis and believe that any reasonably possible change in the key assumptions would not cause the book value of any of the CGU's, or groups of CGU's, to exceed their recoverable amount.

09. LEASES

The Group's leased assets include buildings and plant and equipment. Effective 1 August 2019, the Group adopted NZ IFRS 16 as outlined in the significant accounting policies section, recognising ROU assets and lease obligations of $7.2m. The following table reconciles the Group's lease commitments disclosed in the consolidated financial statements as at 1 August 2019, to the lease obligations recognised on initial application of NZ IFRS 16:

Lease commitments, 31 July 2019	8,902
Recognition exemptions for short-term and low-value leases	(2,444)
Discounted using the incremental borrowing rate at 1 August 2019	(683)
Lease remeasurements	1,417
Lease obligations recognised at 1 August 2019	**7,192**

Lease obligations were measured at the present value of remaining lease payments at the transition date, discounted at the Group's incremental borrowing rate. The Group's weighted average rate applied at 1 August 2019 was 3.49%.

	Buildings $'000	Plant and Equipment $'000	Total $'000
RIGHT-OF-USE ASSETS			
Cost			
Balance as at 1 August 2019	6,726	466	7,192
Additions and acquisitions	6,497	60	6,557
Acquisitions through business combinations (note 18)	8,992	708	9,700
Foreign exchange differences	(9)	-	(9)
Balance as at 31 July 2020	**22,206**	**1,234**	**23,440**
Depreciation			
Balance as at 1 August 2019	-	-	-
Depreciation	4,702	246	4,948
Foreign exchange differences	(5)	-	(5)
Balance as at 31 July 2020	**4,697**	**246**	**4,943**
Carrying amounts			
Balance as at 1 August 2019	6,726	466	7,192
Balance as at 31 July 2020	17,510	987	18,497

	Total $'000
LEASE OBLIGATIONS	
Contractual, undiscounted cash flows associated with the Group's lease obligations are as follows:	
Within one year	5,061
Between one and five years	15,015
Beyond five years	2,443
Total undiscounted lease obligations	**22,519**
Discounted lease obligations recognised on the Company's consolidated balance sheet are as follows:	
Current	4,422
Non-current	14,838
Total discounted lease obligations	**19,260**

Interest expense on lease obligations for the year ended 31 July 2020 was $0.45m and is included in finance expense. Operating lease expenses relating to short-term and low-value leases not included in the measurement of lease obligations for the year ended 31 July 2020 were $1.4m.

DEBT AND EQUITY

The debt and equity section gives information about the Group's capital structure and financing costs related to this structure. This section includes the following notes:

10. FINANCE INCOME AND EXPENSES

Interest income is recognised using the effective interest method. When a loan or receivable is impaired, the Group reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans and receivables is recognised using the original effective interest rate.

Interest expense on borrowings, bank and facility fees and transaction costs are recognised in the income statement over the period of the borrowings, using the effective interest rate method, unless such costs relate to funding capital work in progress. Interest expense on lease obligations are also recognised in the income statement in accordance with NZ IFRS 16, which was adopted by the Group during the period. Refer to Note 9 and Changes in accounting policies for further detail.

	2020 $'000	2019 $'000
Interest income on loans and deposits	134	1,232
Total finance income	**134**	**1,232**
Interest and facility fees	(21,414)	(16,345)
Capitalised borrowing cost	2,089	7,526
Interest on leases	(452)	-
Total finance costs	**(19,777)**	**(8,819)**
Loss on derecognition of financial assets	(1,747)	(1,842)
Net finance costs	**(21,390)**	**(9,429)**

11. LOANS AND BORROWINGS

Interest bearing liabilities are recognised initially at fair value, net of transaction costs incurred. Interest bearing liabilities are subsequently carried at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss component of the statement of comprehensive income over the period of the borrowings using the effective interest method.

	2020			2019		
	Drawn Facility Amount $'000	Transaction Costs $'000	Carrying Amount $'000	Drawn Facility Amount $'000	Transaction Costs $'000	Carrying Amount $'000
Working capital facility NZD	68,910	-	68,910	47,240	-	47,240
Working capital facility USD	33,927	-	33,927	52,386	-	52,386
Current liabilities	**102,837**	**-**	**102,837**	**99,626**	**-**	**99,626**
Retail bonds	180,000	(2,987)	177,013	-	-	-
Revolving credit facility	250,000	(259)	249,741	250,000	(518)	249,482
Non-current liabilities	**430,000**	**(3,246)**	**426,754**	**250,000**	**(518)**	**249,482**

(a) Terms of loans and borrowings

The revolving credit facility and working capital facility within the Group are secured under the terms of the General Security Deed dated 26 June 2013, by which all present and future property is secured to the ANZ Bank and Bank of New Zealand.

The Group facilities include:

- A secured revolving credit facility (Facility A) of $150m maturing on 1 August 2021.
- A secured revolving credit facility (Facility B) of $50m maturing 1 August 2023.
- A secured revolving credit facility (Facility C) of $50m maturing 1 August 2023.
- A secured working capital facility of NZD $320m maturing on 30 September 2020.

The Group recently finalised an additional revolving credit facility of $100m commencing 1 October 2020, stepping down to $70m on 1 January 2021 and maturing 1 May 2021. It also reduced the working capital facility of $320m to $250m and extended it for a period of twelve months and extended revolving credit facility A to 1 October 2021.

The Group is subject to capital requirements imposed by its bank through covenants agreed as part of the lending facility arrangements. The Group has met all externally imposed capital requirements for the twelve months ended 31 July 2020 and 31 July 2019.

Retail Bonds

Borrowings under the retail bond programme are supported by a Master Trust Deed and supplemented by the Series Supplement entered into between the Group and the New Zealand Guardian Trust Company Limited. The retail bonds are unsecured and unsubordinated. At 31 July 2020, the retail bonds had a fair value of $187.7m, based on NZDX valuation.

	Nominal Interest Rate %	Financial Year of Maturity	Carrying Amount 2020	Carrying Amount 2019
Secured revolving credit facility (Facility A, B & C) - ANZ/BNZ	1.48 %	2021, 2023	250,000	250,000
Secured working capital facility - ANZ/BNZ - USD	1.26 %	2020	33,927	52,386
Secured working capital facility - ANZ/BNZ - NZD	1.50 %	2020	68,910	47,240
Subordinated retail bonds	3.83 %	2025	180,000	-

The nominal interest rate is calculated by adding the BKBM rate for NZD facilities, US LIBOR rate for USD facilities and the applicable margin rate. It excludes line fees and swap costs. Nominal interest rate for the subordinated retail bonds excludes transaction costs.

12. SHARE CAPITAL

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new ordinary shares or options are shown in equity as a deduction from the proceeds.

During the reporting period, 83,880 new ordinary shares were granted to participants of the Group's Long Term Incentive scheme as a result of share options that were granted under the scheme vesting and being converted to ordinary shares (2019: nil). These shares were issued to the participants at no cost. Refer to Note 13 for further information.

	2020 Shares	2019 Shares	2020 $'000	2019 $'000
(a) Share capital				
Ordinary shares				
On issue at beginning of period	179,223,028	179,223,028	268,074	268,074
Issue of share capital under employee share plans	83,880	-	470	-
On issue at end of period	**179,306,908**	**179,223,028**	**268,544**	**268,074**

None of the above shares are held by the Group or its subsidiaries.

(b) Ordinary shares

All issued shares are fully paid and have no par value. Ordinary shares are entitled to one vote per share at meetings of Synlait Milk Limited. All ordinary shares rank equally with regard to Synlait Milk Limited's residual assets.

(c) Capital risk management

The Group's capital includes share capital, retained earnings and reserves.

The Group's policy is to maintain a sound capital base so as to maintain investor and creditor confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Group is subject to various security ratios within the bank facilities agreement.

The Group's policies in respect of capital management and allocation are reviewed by the Board of Directors.

(d) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to shareholders by the weighted average number of shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to shareholders and the number of shares outstanding to include the effects of all potential dilutive shares.

Basic EPS for the 2020 financial period was 41.95 cents (2019: 45.89). Diluted EPS for the 2020 financial period was 41.85 cents (2019: 45.77).

13. SHARE BASED PAYMENTS

(a) LTI share scheme

Under the LTI share scheme, participants receive Performance Share Rights ("PSRs") which can be converted into Ordinary Shares in Synlait Milk Limited in three financial years' time provided performance hurdles have been met during the assessment period (the date of award of the PSRs plus three financial years). The number of PSRs granted to participants is set at one quarter of their base salary divided by Synlait Milk Limited's share price on the date of the award of the PSRs.

The PSRs consist of 50% Total Shareholder Return Rights ("TSR Rights") and 50% Earnings Per Share Rights ("EPS Rights"). The vesting for both TSR Rights and EPS Rights is determined in accordance with progressive vesting scales.

Synlait Milk Limited's TSR must be greater than or equal to the 50th percentile of the constituents of the TSR Peer Group over the assessment period for 50% of the TSR Rights to vest, scaled so that 100% of the TSR Rights vest if Synlait Milk Limited's TSR equals or exceeds the 75th percentile of the TSR Peer Group over the assessment period. The TSR Peer Group is determined as at the date of award of the PSRs.

If Synlait Milk Limited's EPS over the assessment period equals a Board approved EPS target, 50% of the EPS Rights vest, scaled so that 100% of the EPS Rights vest if Synlait Milk Limited's EPS over the assessment period equals the Board approved EPS target plus 10%.

For either performance hurdle to be met, Synlait Milk Limited's TSR must be positive over the assessment period. No exercise price is payable upon exercise of a PSR, Synlait Milk Limited's ordinary shares being delivered to a participant for nil consideration. The LTI share scheme is an annual scheme with PSRs granted to Board approved participants each year, noting however that the annual award is assessed over a three year period.

The table below sets out the movement in LTI share scheme PSR's during the year:

	2020	2019
Outstanding 1 August	472,934	506,839
Granted during the year	148,005	134,582
Forfeited during the year	(202,079)	(168,487)
Exercised during the year	(83,880)	-
Total	334,980	472,934

During the period, 83,880 new ordinary shares were granted to participants of the LTI scheme. See Note 12 for further detail.

The fair value of the PSRs awarded at grant date has been determined by an independent third party valuer, using a Monte Carlo simulation to model the total share return for Synlait and the TSR peer group. The fair value of the PSRs awarded, along with key assumptions, are listed below:

	2020 PSRs	2019 PSRs
Risk free rate	0.83 %	1.97 %
Volatility	37.70 %	35.84 %
Share price at entitlement date	9.79	10.81
Share price at grant date	9.18	8.66
Total value of options granted at grant date ($000's)	783	559

The estimated value of the PSRs is amortised over the vesting period from grant date.

(b) Expenses arising from share based payment transactions

Total expenses arising from share based payment transactions recognised during the period as part of employee benefit expense were as follows:

	2020	2019
	$'000	$'000
Expenses for equity settled share based payment transactions	523	644

14. RESERVES AND RETAINED EARNINGS

(a) Retained earnings

Movements in retained earnings were as follows:

		Group
	2020	2019
	$'000	$'000
Balance 1 August	248,775	166,536
Net profit for the year	75,208	82,239
Balance 31 July	323,983	248,775

(b) Nature and purpose of reserves

(i) Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value hedging instruments and the cost of cash flow hedging instruments. Cash flow hedging instruments relate transactions that have not yet occurred.

(ii) Employee benefits reserve

The current year movement in the employee benefits reserve of ($0.3m) is comprised of the cumulative share based payment expense for share options not yet vested of $0.5m (2019: $0.6m), vesting of rights during the period of ($0.5m) (2019: $nil) and the related movement in deferred tax asset of ($0.3m) (2019: $0.1m)

(c) Dividends

No dividends were declared by the Group during the year.

FINANCIAL RISK MANAGEMENT

The financial risk management section presents information about the Group's financial risk exposures and the financial instruments used to mitigate this. This section includes the following notes:

15. FINANCIAL RISK MANAGEMENT

The Group enters into a variety of derivative financial instruments to manage its exposure to interest rate risk, foreign exchange rate risk, and commodity price risk including forward exchange contracts, interest rate swaps and commodity derivative contracts.

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, interest rate risk and commodity price risk), credit risk and liquidity risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

On 1 April 2020, the Group completed the acquisition of 100% of the shares of Dairyworks Limited ("Dairyworks"). See Note 18 for further details. The acquisition has introduced additional financial risks similar to the financial risks of the Group. Dairyworks currently has its own separate treasury policy from the Group's policy with the need for its own risk management parameters to reflect the business and markets that it operates in. Any deviation in Dairyworks' policy from the Group is made explicit in the notes below.

Market risk

Foreign exchange risk

The Group is exposed to foreign currency risk on its sales, which are predominantly denominated in US dollars. The Group is also exposed to foreign currency risk on the purchase of raw materials for production and capital equipment purchases from overseas. The Group enters into derivative arrangements in the ordinary course of business to manage foreign currency risk. These instruments include forward exchange contracts, option collars and vanilla options. These instruments enable the Group to mitigate the risk the variable exchange rates present to future cash flows for sales receipts or purchases by fixing or limiting the exchange rate at which these cash receipts or payments are exchanged into NZ dollars.

In relation to foreign exchange contracts are entered into based on forecast cash receipts or payments, variability in the expected timing or amounts of future cash flows can lead to ineffective hedging. To mitigate the risk of ineffectiveness the Group's policy is to hedge a decreasing proportion of the risk exposure the further into the future the exposure exists given the increasing uncertainty of cash flows. Additionally the Group's policy is that the proportion of risk exposure to be hedged changes on a monthly basis in response to the movement in market rates. As at 31 July 2020, the Group has hedged 62% of its exposure to foreign exchange risk on sales, and 23% of its exposure to foreign exchange risk on payables, over the following 2 years.

In addition to the above exposure, Dairyworks had entered USD $2.8m of foreign exchange contracts for confirmed purchase of raw materials for production payable within several months of reporting date.

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

Interest rate risk

Interest rate risk is the risk that the value of the Group's assets and liabilities will fluctuate due to changes in market interest rates. The Group is exposed to interest rate risk primarily through its bank overdrafts and borrowings.

The Group manages its interest rate risk by using interest rate swaps to convert a portion of its floating rate debt to fixed interest rates in relation to the benchmark interest rate element. As interest rate swaps are entered into based on forecast debt levels, variability in future cash flows and debt levels can lead to ineffective hedging. To mitigate the risk of ineffectiveness the Group's policy is to hedge a decreasing proportion of the risk exposure the further into the future the exposure exists given the increasing uncertainty of cash flows.

The Group has a Board approved treasury policy that sets the parameters to the extent of the cover taken. The policy requires the Group to hedge 30% to 80% of its exposure to interest rate risk that matures within 3 years, 20% to 60% of the risk that matures between 3 and 5 years, and 0% to 40% of the risk that matures between 5 and 10 years.

Commodity Price Risk

Dairy commodity price risk is the risk of volatility in profit and loss from the movement in dairy commodity prices to which the Group may be exposed. Volatility in global dairy commodity prices can have an adverse impact on the Groups earnings and milk price by eroding selling prices and increasing input costs.

The Group primarily manages its dairy commodity price risk by:

- Determining the most appropriate mix of products to manufacture based on the milk supply curve and global demand for dairy products;
- Governing the length and terms of sales contracts so that sales revenue is reflective of current market prices and is, where appropriate, linked to Global Dairy Trade (GDT) prices; and
- Using commodity derivative contracts to manage sales price volatility caused by fluctuations in GDT prices.

The Group has a Board approved treasury policy that sets the parameters under which commodity cover is to be taken, including permitted derivative types and volume limits.

Credit risk

The Group's exposure to credit risk is mainly influenced by its customer base and banking counterparties. Management has a credit policy in place under which each new customer is rigorously analysed for credit worthiness. Investments and derivatives are only entered into with reputable financial banks.

The carrying amount of financial assets represents the Group's maximum credit exposure. The Group also retains all the late payment risk in the derecognition of financial assets, as described in note 4.

Synlait Milk Limited guarantees all facilities held by Synlait Milk Finance Limited.

Liquidity risk

Liquidity risk represents the Group's ability to meet its contractual obligations as they fall due. The Group evaluates its liquidity requirements on an ongoing basis and uses a variety of facilities to manage liquidity risk. The Group has negotiated banking facilities sufficient to meet its medium term facility requirements.

The Group has internal limits in place in order to reduce exposure to liquidity risk, as well as having committed lines of credit. It is the Group's policy to provide credit and liquidity enhancements only to wholly owned subsidiaries.

Market risk

(i) Foreign exchange risk

The Group's exposure to foreign currency risk at the reporting date was as follows:

				2020				2019
	USD	AUD	EUR	RMB	USD	AUD	EUR	RMB
	$'000	$'000	$'000	$'000	$'000	$'000	$'000	$'000
Trade receivables	23,039	3,479	-	-	34,462	36	-	18
Trade payables	(7,142)	(605)	(243)	-	(363)	-	(11)	-
Working capital facility	(22,487)	-	-	-	(34,300)	-	-	-

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

The Group's exposure to foreign currency in the period ended 31 July 2020 is limited to its sales of dairy products, purchases of raw materials for production, capital equipment purchases and USD working capital facility. As at the reporting date, the Group had the following foreign exchange derivative instruments outstanding in respect of future sales and purchases transactions:

	2020		2019	
	Weighted Average Exchange Rate	Nominal Balance USD$'000	Weighted Average Exchange Rate	Nominal Balance USD$'000
Exports				
Less than 1 year	0.6478	379,500	0.6895	353,150
1 to 2 years	0.6318	192,050	0.6765	160,600
Imports				
Less than 1 year	0.6368	(46,021)	0.6752	(42,467)

(ii) Interest rate risk

As at the reporting date, the Group had the following interest rate swap contracts outstanding:

	2020		2019	
	Weighted Average Interest Rate %	Nominal Balance $'000	Weighted Average Interest Rate %	Nominal Balance $'000
Less than 1 year	4.26 %	57,250	4.23 %	79,500
1 to 2 years	4.36 %	40,000	4.26 %	57,250
2 to 3 years	4.36 %	40,000	4.36 %	40,000
3 to 4 years	4.20 %	30,000	4.36 %	40,000
4 to 5 years	3.54 %	15,000	4.20 %	30,000
5 to 6 years	3.56 %	10,000	3.54 %	15,000
6 to 7 years	-%	-	3.56 %	10,000

The above balances include forward start swap contracts for various periods and do not necessarily reflect the current active contracts held at any one point in time.

In managing interest rate risks, the Group aims to reduce the impact of short term fluctuations on the Group's earnings. Over the longer term, however, changes in interest rates will have an impact on profit.

(iii) Sensitivity analysis

The following table summarises the sensitivity of the Group's profit and equity to interest rate risk and foreign exchange risk.

The sensitivity analysis below has been determined based on the mark to market impact on financial instruments of changing interest and foreign exchange rates at balance date. The analysis is prepared assuming the amount of the financial instrument outstanding at the balance sheet date was outstanding for the whole year, and by adjusting one input whilst keeping the others constant.

	Post-tax impact on the income statement		Post-tax impact on cash flow hedge reserve (equity)	
	2020 $'000	2019 $'000	2020 $'000	2019 $'000
Interest rates				
100 basis point increase in interest rate	(2,879)	(2,185)	1,252	1,764
100 basis point decrease in interest rate	2,879	2,185	(1,303)	(1,843)
Foreign exchange rates				
5% increase in exchange rate	-	-	27,127	23,985
5% decrease in exchange rate	-	-	(29,966)	(26,504)

(iv) Commodity derivatives

During the reporting period the Group entered into a small number of commodity derivative contracts to further support the Group's existing financial risk management strategy. The movement in the fair value of the commodity derivatives is included within the cash flow hedge reserve.

Liquidity risk

The total repayments and associated maturity of financial liabilities as at balance date is reported below.

	Less than 12 months $'000	Between 1 and 2 years $'000	Between 2 and 5 years $'000	Over 5 years $'000	Total $'000
At 31 July 2020					
Working capital facility	102,837	-	-	-	102,837
Trade and other payables	238,770	-	-	-	238,770
Loans and borrowings	-	149,790	276,964	-	426,754
Derivative financial instruments	14,148	835	2,782	1,188	18,953
Lease liabilities	4,422	3,206	8,106	3,525	19,260
Total	**360,177**	**153,831**	**287,852**	**4,713**	**806,574**
At 31 July 2019					
Working capital facility	99,626	-	-	-	99,626
Trade and other payables	216,020	-	-	-	216,020
Loans and borrowings	-	149,580	99,902	-	249,482
Derivative financial instruments	27,960	6,569	3,201	916	38,647
Total	**343,606**	**156,149**	**103,103**	**916**	**603,775**

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

Cash flow hedges

The Group enters into cash flow hedges of highly probable forecast transactions and firm commitments, as described in accounting policy section of this note.

Hedging instruments used in cash flow hedges	Nominal Amount	Carrying Amount		Hedge Accounted Amounts in Cash Flow Reserve	Total Cash Flow Hedge Reserve
		Assets	Liabilities	Intrinsic Value	
	$'000	NZD$'000	NZD$'000	NZD$'000	NZD'000
31 July 2020					
Foreign exchange risk					
Foreign exchange contracts (USD)	528,337	36,419	12,078	24,341	**24,341**
Interest rate risk					
Interest rate swaps	57,250	-	6,777	(6,777)	**(6,777)**
Commodity price risk					
Dairy commodity futures (NZD)	12,016	195	-	-	**-**
Total		36,614	18,855	17,564	**17,564**
At 31 July 2019					
Foreign exchange risk					
Foreign exchange contracts (USD)	471,283	2,320	31,531	(29,211)	**(29,211)**
Interest rate risk					
Interest rate swaps	79,500	-	7,116	(7,116)	**(7,116)**
Commodity price risk					
Dairy commodity futures (NZD)	5,307	83	-	-	**8**
Total		**2,403**	**38,647**	**(36,327)**	**(36,319)**

The above table does not include USD $2.8m foreign exchange contracts held by Dairyworks as it has not elected to cash flow hedge.

Hedging instruments are located within the derivative financial instruments line items in the statement of financial position, classified as assets or liabilities, current or non-current.

	2020		2019	
Effects of Cash Flow Hedges on Statement of Comprehensive Income	**Hedging Gains/(losses) Recognised in Other Comprehensive Income $'000**	**Hedge Ineffectiveness Recognised in Profit or Loss $'000**	Hedging Gains/(losses) Recognised in Other Comprehensive Income $'000	Hedge Ineffectiveness Recognised in Profit or Loss $'000
Foreign exchange risk				
Forward exchange contracts	**53,551**	**-**	(19,703)	-
Foreign currency collars	**-**	**-**	154	-
Interest rate risk				
Interest rate swaps	**339**	**-**	(1,578)	-
Commodity price risk				
Dairy commodity futures (NZD)	**(8)**	**(299)**	(196)	-
Total	**53,882**	**(299)**	**(21,323)**	-

Impact to reserves in equity

The impact of the Group's hedge accounting policies on the reserves in equity is presented in the table below:

	2020	2019
Hedge Reserves	**$'000**	$'000
Opening balance	**(26,148)**	**(10,796)**
Movements attributable to cashflow hedges:		
Change in value of effective derivative hedging instruments	**16,841**	(29,589)
Reclassifications to the income statement as hedged transactions occurred	**37,041**	8,266
Tax (credit)/expense	**(15,087)**	5,971
Total movement	**38,795**	**(15,352)**
Closing balance	**12,647**	**(26,148)**

16. FINANCIAL INSTRUMENTS

Classification

The Group classifies its financial assets in three categories: at amortised cost, at fair value through other comprehensive income and at fair value through profit or loss. The classification of financial assets depends on the business model within which the financial asset is held and its contractual cash flow characteristics.

The Group classifies its financial liabilities in two categories: at amortised cost and at fair value through profit or loss.

(i) Financial instruments at amortised cost

Financial assets are classified as measured at amortised cost if the Group's intention is to hold the financial assets for collecting cash flows and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest.

The Group currently classifies its cash and cash equivalents, restricted cash equivalents, accounts receivable and other receivables as financial assets measured at amortised cost.

Financial liabilities are classified as measured at amortised cost using the effective interest method, with the exception of those classified at fair value.

The Group currently classifies its accounts payable, accrued liabilities (excluding derivatives) and term debt as financial liabilities measured at amortised cost.

(ii) Financial instruments at fair value through other comprehensive income ("FVOCI")

The Group has elected to designate certain investments in equity instruments that are not held for trading as FVOCI at initial recognition and to present gains and losses in other comprehensive income. Dividends earned from such investments are recognised in profit or loss.

(iii) Financial instruments at fair value through profit or loss ("FVPL")

Financial assets that do not meet the criteria for classification as measured at either amortised cost or FVOCI are classified as FVPL.

Derivative financial instruments that are not in an effective hedge relationship are classified as FVPL.

Recognition and measurement

The Group recognises a financial asset or a financial liability when it becomes a party to the contractual provisions of the instrument.

Regular purchases and sales of financial assets are recognised on the trade date – the date on which the Group commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not classified at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the profit and loss component of the statement of comprehensive income.

Where financial assets are subsequently measured at amortised cost, interest revenue, credit losses and foreign exchange gains or losses are recognised in profit or loss. On derecognition, any gain or loss is recognised in profit or loss. Financial liabilities subsequently measured at amortised cost are measured using the effective interest method.

Where investments in equity instruments are designated as FVOCI, fair value gains and losses are recognised in other comprehensive income. Dividends earned from such investments are recognised in profit or loss.

Where financial assets are subsequently measured at FVPL, all gains and losses are recognised in profit or loss.

A key management judgement is the assessment that substantially all the risks and rewards of ownership have been transferred in the derecognition of financial assets.

Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

Financial liabilities are derecognised when the contractual obligations are discharged, cancelled or expired.

Fair value estimation

The fair value of financial assets and financial liabilities must be estimated for recognition and measurement or for disclosure purposes.

As the Group's financial instruments, with the exception of retail bonds, are not traded in active markets their fair value is determined using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance date.

All financial instruments held at fair value are included in level 2 of the valuation hierarchy as defined in NZ IFRS 13, with the exception of the retail bonds, which are included in level 1. The retail bonds are listed instruments on the NZDX and the Group is satisfied there is sufficient trading in these instruments to qualify as an active market.

16. FINANCIAL INSTRUMENTS (CONTINUED)

The fair value of foreign currency forward contracts is determined using forward exchange rates at balance date. The fair value of foreign exchange option agreements is determined using forward exchange rates at balance date. The fair value of interest rate swaps is determined using forward interest rates as at reporting date. The fair value of commodity derivatives is determined using NZX settlement prices.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a current legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously. There are master netting agreements in place for derivative financial instruments held, however these instruments have not been offset in the statement of financial position as they do not currently meet the criteria for offset.

Impairment of financial assets

The Group has adopted the expected credit loss ("ECL") model. For further detail please refer to Note 4. The Group assesses whether there is evidence that a financial asset or group of financial assets is impaired, with the exception of assets that are fair valued through profit or loss. A financial asset or a group of financial assets can be impaired and the impairment losses are recognised in accordance with IFRS 9. The Group continues to assess if historical and future objective evidence of impairment exists after the initial recognition of the asset.

Derivative financial instruments - hedge accounting

The Group enters into a variety of derivative financial instruments to manage its exposure to interest rate risk, foreign exchange rate risk, and commodity price risk including forward exchange contracts, interest rate swaps, and commodity derivative contracts.

Derivatives are initially recognised at fair value at the date the derivative contact is entered into and are subsequently remeasured to fair value at each reporting date. For derivatives measured at fair value, the gain or loss that results from changes in fair value of the derivative is recognised in earnings immediately, unless the derivative is designated and effective as a hedging instrument. Hedges of highly probable forecast transactions or hedges of foreign currency risk of firm commitments are designated as cash flow hedges by the Group, with the exception for Dairyworks.

The full fair value of a hedging derivative is classified as a current asset or liability when the remaining term of the hedged item is 12 months or less from balance date, or when cash flows arising from the hedged item will occur within 12 months or less from balance date. The full fair value of a hedging derivative is classified as a non-current asset or liability when the remaining maturity of the hedged item is more than 12 months and no cash flows will occur within 12 months of balance date.

(i) Hedge accounting

The Group designates certain hedging instruments in respect of foreign currency risk and interest rate risk as cash flow hedges. Hedges of risk on firm commitments and highly probably transactions are accounted for as cash flow hedges.

At the inception of the hedge relationship, the Group documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in fair values or cash flows of the hedged item.

(ii) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in other comprehensive income and accumulated as a separate component of equity in the hedging reserve. The gain or loss relating to the ineffective portion and reclassification adjustments are recognised immediately in profit or loss, included in revenue for foreign exchange instruments and commodity price derivatives, and finance costs for interest rate swaps.

Amounts recognised in the hedging reserve are classified from equity to profit or loss (as a reclassification adjustment) in the periods when the hedged item is recognised in profit or loss, in the same line as the recognised hedged item.

Hedge accounting is discontinued when the Group revokes the hedging relationships, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss recognised in the hedging reserve at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in the hedging reserve is immediately recorded in profit or loss.

The Group separates the intrinsic value and time value of vanilla option and collar contracts, designating only the intrinsic value as the hedging instrument. The time value, including any gains or losses, is recognised in other comprehensive income until the hedged transaction occurs and is recognised in profit or loss.

(iii) Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the income statement.

16. FINANCIAL INSTRUMENTS (CONTINUED)

(a) Financial instruments by category

Financial assets	At Amortised Cost $'000	At Fair Value Through Other Comprehensive Income $'000	At Fair Value Through Profit or Loss $'000	Total $'000
At 31 July 2020				
Cash and cash equivalents	5,887	-	-	5,887
Derivative financial instruments	-	-	36,614	36,614
Trade and other receivables	63,057	-	-	63,057
Instruments in equity	-	143	-	143
Total	**68,944**	**143**	**36,614**	**105,701**
At 31 July 2019				
Cash and cash equivalents	16,007	-	-	16,007
Derivative financial instruments	-	-	2,403	2,403
Trade and other receivables	61,933	-	-	61,933
Instruments in equity	-	110	-	110
Total	**77,940**	**110**	**2,403**	**80,453**

Financial liabilities	At Amortised Cost $'000	At Fair Value Through Profit or Loss $'000	Total $'000
At 31 July 2020			
Derivative financial instruments	-	18,953	18,953
Working capital facility	102,837	-	102,837
Trade and other payables	238,770	-	238,770
Borrowings	426,754	-	426,754
Total	**768,361**	**18,953**	**787,314**
At 31 July 2019			
Derivative financial instruments	-	38,647	38,647
Working capital facility	99,626	-	99,626
Trade and other payables	216,020	-	216,020
Borrowings	249,482	-	249,482
Total	**565,128**	**38,647**	**603,775**

All derivative financial instruments are designated in effective hedge relationships, with exception for derivative financial instruments held by Dairyworks.

For instruments held at amortised cost, carrying amount is considered a reasonable approximation for fair value, with exception to the Retail Bond.

OTHER

This section contains additional information regarding the performance of the group during the financial year. This section includes the following notes:

17. INCOME TAX

The tax expense for the period comprises current and deferred tax. Tax is recognised in the profit and loss component of the statement of comprehensive income, except to the extent that it relates to items recognised in either other comprehensive income or directly in equity. In these cases, the tax is also recognised in other comprehensive income or directly in equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

New Zealand tax consolidated group

Synlait Milk Limited and its wholly-owned New Zealand controlled entity, Synlait Milk Finance Limited, form a tax consolidated group. The New Zealand Dairy Company Limited, Eighty Nine Richard Pearse Drive Limited, Synlait Foods (Talbot Forest) Limited and Dairyworks Limited are not members of the tax consolidated group.

	2020 $'000	2019 $'000
(a) Income tax expense		
Current tax expense		
Current tax on profits for the year	(21,614)	(29,220)
Current tax on prior period adjustments	4,212	721
Total	**(17,402)**	**(28,499)**
Deferred tax expense		
Temporary differences	(7,070)	(3,433)
Changes in tax rates and laws	2,229	-
Prior year adjustments	(4,473)	(925)
Tax losses to carry forward	23	17
Total deferred tax	**(9,291)**	**(4,341)**
Income tax expense	**(26,693)**	**(32,840)**
(b) Reconciliation of effective tax rate		
Profit before income tax	101,901	115,079
Income tax using the Group's domestic tax rate - 28%	(28,532)	(32,222)
Non-deductible costs	(889)	(533)
Total	**(29,421)**	**(32,755)**
Prior year adjustments	(261)	(85)
Deferred tax credit relating to changes in tax rates and laws	2,229	-
Research and development tax credit	779	-
Other tax effects for reconciliation between accounting profit and tax expense	(19)	-
Total	**2,728**	**(85)**
Income tax expense	**(26,693)**	**(32,840)**

As part of the New Zealand Government's COVID-19: Economic Response Package, depreciation deductions will be reintroduced for new and existing industrial and commercial buildings from the 2020/21 tax year. The Group have determined that, as a result of this legislative change, the tax base of certain assets has increased, reducing a taxable temporary difference (deferred tax liability) previously recognised. The impact of these changes has resulted in a reduction in deferred tax liabilities and a reduction in tax expense of $2.2m.

	2020 $'000	2019 $'000
(c) Imputation credits		
Imputation credits available directly and indirectly to the shareholders of the Group	**98,009**	**83,219**

17. INCOME TAX (CONTINUED)

(d) Income tax recognised in other comprehensive income

The tax (charge)/credit relating to components of other comprehensive income is as follows:

	Before Tax $'000	Tax (Expense)/Benefit $'000	After Tax $'000
31 July 2020			
Cash flow hedges	53,882	(15,087)	38,795
Other comprehensive income subject to tax	53,882	(15,087)	38,795
31 July 2019			
Cash flow hedges	(21,323)	5,971	(15,352)
Other comprehensive income subject to tax	(21,323)	5,971	(15,352)

(e) Deferred taxation

The balance comprises temporary differences attributable to:

	2020 $'000	2019 $'000 (restated)
Assets		
Derivatives	-	10,170
Tax losses carried forward	23	112
Other items	2,793	2,128
Total deferred tax assets	2,816	12,410
Liabilities		
Property, plant and equipment	(47,632)	(37,444)
Derivatives	(4,918)	-
Intangible assets	(4,913)	-
Total deferred tax liabilities	(57,463)	(37,444)
Total deferred tax	(54,647)	(25,034)

Movements - Group	Balance 1 Aug 2018 $'000 (restated)	Recognised in Profit or Loss $'000	Recognised in Other Comprehensive Income $'000	Recognised Directly in Equity $'000	Recognised from a Business Combination $'000	Prior Year Adjustment $'000	Balance 31 July 2019 $'000
Property, plant and equipment	(32,528)	(4,165)	-	-	-	(751)	(37,444)
Derivatives	4,199	-	5,971	-	-	-	10,170
Other items	1,287	603	-	84	-	155	2,128
Tax losses carried forward	295	(178)	-	-	-	(5)	112
Total	(26,747)	(3,740)	5,971	84	-	(602)	(25,034)

Movements - Group	Balance 1 Aug 2019 $'000	Recognised in Profit or Loss $'000	Recognised in Other Comprehensive Income $'000	Recognised Directly in Equity $'000	Recognised from a Business Combination $'000	Prior Year Adjustment $'000	Balance 31 July 2020 $'000
Property, plant and equipment	(37,444)	(5,921)	-	-	227	(4,495)	(47,633)
Derivatives	10,170	-	(15,087)	-	-	-	(4,918)
Other items	2,128	1,080	-	(389)	(160)	134	2,793
Tax losses carried forward	112	23	-	-	-	(112)	23
Intangible assets	-	-	-	-	(4,912)	-	(4,912)
Total	(25,034)	(4,818)	(15,087)	(389)	(4,845)	(4,473)	(54,647)

The opening deferred tax balance relating to Plant, Property and Equipment for the year ended 31 July 2019 has been restated to correct an immaterial prior period error which was identified during the current year. Please refer to Note 18 for further detail.

18. BUSINESS COMBINATIONS

Acquisitions of businesses are accounted for using the acquisition method. The cost of the acquisition is measured at fair value, which is calculated as the sum of the assets given, liabilities incurred or assumed, and equity instruments issued by the Group, at acquisition date, in exchange for control of the acquiree. Acquisition related costs are recognised in profit or loss as incurred. The results of subsidiaries acquired or disposed of during the year are included in the Consolidated Income Statement from the date of acquisition or up to the date of disposal as appropriate.

(a) Talbot Forest Cheese Limited

On 1 August 2019, the Group completed the acquisition of selected assets and liabilities of Talbot Forest Cheese Ltd ("TFC") for total consideration of $38.3m, including inventory. The acquirer was a newly incorporated company, Synlait Foods (Talbot Forest) Limited. On the acquisition date, the Group paid $18.8m. Of the remaining consideration payable, $18.1m was applied against an intercompany loan owed by the vendor to the Group and the remaining $1.4m was paid over the course of FY20 upon completion of pre-completion works and plant acceptance tests. The acquisition has been accounted for in accordance with IFRS 3, Business Combinations.

The acquisition of TFC includes a cheese manufacturing plant located in Temuka, New Zealand, capable of manufacturing a variety of cheese products with an annual production capacity of 12,000MT, along with a consumer cheese brand. The acquisition excludes the Talbot Forest Cheese artisan factory in Geraldine, New Zealand.

The following summarises the consideration paid for TFC and amounts of assets acquired and liabilities assumed recognised at the acquisition date:

	August 1, 2019
	$'000
Current Assets	
Inventory	2,520
Non-current Assets	
Property, plant and equipment	12,745
Land and buildings	5,960
Brand	1,700
Non-current Liabilities	
Deferred Tax	(708)
Total identifiable net assets at fair value	**22,217**
Goodwill arising on acquisition	16,132
Total consideration	**38,349**
Less: Debt and accrued interest payable owed to the Group extinguished upon acquisition	(18,077)
Net cash outflow on acquisition	**20,272**

The land, buildings, plant and equipment, inventory, and brand have been recognised at acquisition date fair values based on third party valuations. Goodwill arose in the acquisition of the business operations of TFC because the cost of acquisition reflected the benefit of future cash flows above the current fair market value of the assets acquired, and the synergies and future market benefits expected to be obtained from the cheese manufacturing plant and related brand.

Acquisition costs of $0.1m and $0.3m have been recognised in the income statements for the years ended 31 July 2020 and 31 July 2019, respectively.

Impact of the acquisition on the results of the Group

From the date of acquisition, TFC has contributed $11.5m to revenue and a loss of ($4.7m) to net profit after tax. Had the combination not taken place, revenue of the Group from continuing operations would have been $1,290.5m, and the net profit from continuing operations for the Group would have been $79.9m.

(b) Dairyworks Limited

On 1 April 2020, the Group completed the acquisition of 100% of the shares of Dairyworks Ltd. ("Dairyworks"). The purchase price of Dairyworks was $112 million on the basis of a debt and cash-free business. The acquisition was priced using a locked box mechanism whereby the equity price of Dairyworks was determined or "locked-in" based on an effective date balance sheet of 30 September 2019.

Debt, working capital, and other purchase price adjustments, based on the 30 September 2019 locked box adjustments resulted in final consideration of $63.6m being transferred to the vendors of Dairyworks. Immediately following acquisition, the Group repaid $43.0m of outstanding debt and accrued interest which was assumed as part of the acquisition, utilising existing banking facilities.

Dairyworks' operations are located in Christchurch, New Zealand. It specialises in the processing, packaging, and marketing of dairy products including cheese, butter, ice cream, and milk powder through it's four brands Alpine, Rolling Meadow, Dairyworks, and Deep South. Dairyworks is one of the largest sellers of everyday dairy products in the New Zealand consumer market.

The acquisition has been accounted for in accordance with IFRS 3, Business Combinations. The following summarises the consideration paid for Dairyworks and fair values of assets acquired and liabilities assumed recognised at the acquisition date.

18. BUSINESS COMBINATIONS (CONTINUED)

	August 1, 2020
	$'000
Current Assets	
Cash and cash equivalents	10,932
Trade receivables	26,508
Inventory	31,474
Other current assets	413
Non-current Assets	
Intangible assets	530
Deferred tax assets	472
Capital work in progress	233
Property, plant and equipment	15,336
Right-of-use assets	9,700
Brands	15,845
Current Liabilities	
Trade and other payables	(29,137)
Current tax liabilities	(4,573)
Loans and borrowings	(43,224)
Lease liability - current	(1,399)
Non-current Liabilities	
Deferred tax liabilities attributable to fair value differentials	(4,609)
Lease liability - non-current	(8,301)
Total identifiable net assets at fair value	**20,200**
Goodwill arising on acquisition	43,387
Total consideration	**63,587**
Purchase price	112,000
Less: Effective date adjustment for working capital and net debt	(40,441)
Less: Interim period and other adjustments	(7,972)
Total consideration transferred	**63,587**
Less: Cash and cash equivalents acquired	(10,932)
Net cash outflow on acquisition	**52,655**

The land, buildings, plant and equipment, inventory, and brands have been recognised at acquisition date fair values based on third party valuations. Right of use assets have been recognised at acquisition date present values of remaining lease payments.

The acquisition gave rise to brand assets for the Rolling Meadow, Alpine, Dairyworks, and Deep South brands. The brands were valued using the relief from royalty method. Key assumptions used in the valuation of the brand assets were: notional royalty rate (25.0%), annual revenue growth rate (2.0% to 5.2%), post-tax discount rate (13.5%), and terminal growth rate (2.0%).

Goodwill arose in the acquisition of the business operations of Dairyworks because the cost of acquisition reflected the benefit of future cash flows above the current fair market value of the assets acquired, and the synergies and future market benefits expected to be obtained from Dairyworks' operations and related brands.

Acquisition costs of $0.8m and $0.1m have been recognised in the income statements for the years ended 31 July 2020 and 31 July 2019, respectively.

Impact of the acquisition on the results of the Group

From the date of acquisition, Dairyworks has contributed $81.5m to revenue and $2.5m to net profit after tax. Had the combination not taken place, revenue of the Group from continuing operations would have been $1,220.5m, and the net profit from continuing operations for the Group would have been $72.7m. Had the acquisition occurred on 1 August 2019, revenue of the Group would have been $1,465.8m and net profit would have been $79.0m.

During FY20 the Group began to leverage synergies between Synlait Foods (Talbot Forest) Limited and Dairyworks by establishing an integrated cheese value chain. For the purposes of goodwill impairment testing, the Group has treated Synlait Foods (Talbot Forest) Limited and Dairyworks as a single consumer food service cash generating unit. See Note 8 for further detail on goodwill and impairment testing.

(c) Prior Period Error

During the year, an immaterial prior period error was identified in relation to the recognition of the acquisition of Eighty-Nine Richard Pearse Drive Limited (see Note 17 in the Group financial statements for the year ended 31 July 2017 for further information on the acquisition).

As part of the acquisition, a building was acquired which was non-depreciable for tax purposes as it had an estimated useful life of 50 years or greater (building cost of $8.5m). A deferred tax liability was not recognised on the building in accordance with NZ IAS 12 Income Taxes and NZ IFRS 3 Business Combinations as the initial recognition exemption was incorrectly applied. Had a deferred tax liability been recognised, goodwill recognised on the acquisition would have increased by $2.4m.

The Group has elected to correct the error in the current period to ensure accuracy of these balances going forward. Each of the affected financial statement line items for the prior periods have been restated as follows

	2017	2018	2019	2020
Balance sheet (extract)	$'000	$'000	$'000	$'000
Goodwill	2,383	2,383	2,383	2,383
Deferred tax liabilities	(2,383)	(2,383)	(2,383)	(2,383)
Increase/(decrease) to net assets	-	-	-	-

This error has had no impact on either the earnings per share or diluted earning per share of the Group in any of the reporting periods affected.

19. OTHER INVESTMENTS

Investments in associates

Associates are those entities in which the Group, either directly or indirectly, holds a significant but not a controlling interest, and has significant influence. Investments in associates are accounted for using the equity method and are measured in the statement of financial position at cost plus post acquisition changes in the Group's share of net assets. Goodwill relating to associates is included in the carrying amount of the investment. Dividends reduce the carrying value of the investment.

	2020 $'000	2019 $'000
Equity securities	110	110
Investment in associates	33	-
Total other investments	**143**	**110**

Synlait Milk Limited held, either directly or indirectly, interests in the following entities at the end of the reporting period:

			Equity Holding	
Name of entity	Country of Incorporation	Class of Shares	2020 %	2019 %
Synlait Milk Finance Limited (Subsidiary)	New Zealand	Ordinary	100	100
The New Zealand Dairy Company Limited (Subsidiary)	New Zealand	Ordinary	100	100
Eighty Nine Richard Pearse Drive Limited (Subsidiary)	New Zealand	Ordinary	100	100
Sichuan New Hope Nutritional Foods Co. Ltd (Associate)	China	Ordinary	25	25
Synlait Business Consulting (Shanghai) Limited (Subsidiary)	China	Ordinary	100	100
Synlait Foods (Talbot Forest) Limited (Subsidiary)	New Zealand	Ordinary	100	-
Dairyworks Limited (Subsidiary)	New Zealand	Ordinary	100	-
Dairyworks (Australia) Pty Limited (Subsidiary)	Australia	Ordinary	100	-

Associates

In January 2015, the Group acquired 25% of the shares of Sichuan New Hope Nutritionals, an infant formula company registered in China. This company owns and markets the "Akara" and "E-Akara" infant formula brands in the Chinese market, which are exclusively manufactured by Synlait Milk Limited.

The investment is not individually significant to the Group. The Group's share of this equity accounted investment is as follows:

	2020 $'000	2019 $'000
Gain/(loss) from continuing operations	33	(580)
Total	**33**	**(580)**

The carrying value of the investment in New Hope Nutritionals at balance date:

	2020 $'000	2019 $'000
Opening balance	-	580
Share of gains/(losses)	33	(580)
Total	**33**	-

20. RELATED PARTY TRANSACTIONS

Parent entity

Bright Dairy Holding Limited hold 39.02% of the shares issued by Synlait Milk Limited (2019: 39.04%). Bright Dairy Holding Limited is a subsidiary of Bright Food (Group) Co. Limited, a State Owned Enterprise domiciled in the Peoples' Republic of China.

Other related entities

In June 2013, a subsidiary of Synlait Milk Limited, Synlait Milk Finance Limited, was set up primarily for holding all banking facilities for the Group and related interest rate swaps. Funds are loaned to Synlait Milk Limited and interest is charged at market rates.

In January 2015, the Group acquired 25% of the shares of Sichuan New Hope Nutritionals, an infant formula company registered in China. This company owns and markets the "Akara" and "E-Akara" infant formula brands in the Chinese market, which are exclusively manufactured by Synlait Milk Limited. New Hope Innovation (Hong Kong) Trading Company Limited is a related entity of Sichuan New Hope Nutritionals and is engaged in the import and export of dairy foods. Main products include whole milk powder, skim milk powder and whey powder. The company is the Hong Kong operations of the Chinese New Hope Dairy group, New Hope Dairy.

In May 2017 Synlait Milk Limited acquired 100% of the share capital of The New Zealand Dairy Company Limited and Eighty Nine Richard Pearse Drive Limited. The New Zealand Dairy Company Limited was constructing a blending and canning plant in Auckland, which was subsequently sold to Synlait Milk Limited. The New Zealand Dairy Company Limited is now a non-trading entity. Eighty Nine Richard Pearse Drive Limited owns the land and buildings at which the Auckland blending and canning plant was constructed. Eighty Nine Richard Pearse Drive Limited leased its land and buildings to The New Zealand Dairy Company Limited, and now leases them to Synlait Milk Limited.

In May 2019, Synlait Business Consulting (Shanghai) Limited was incorporated. The wholly owned foreign entity started operations from 1 August 2019 and the principal activity of the entity is to provide services to assist Synlait to market products in China.

In August 2019, the Group acquired selected assets and liabilities of Talbot Forest Cheese Limited. The acquirer was a newly incorporated company, Synlait Foods (Talbot Forest) Limited. Synlait Foods (Talbot Forest) Limited manufactures a variety of cheese products. Synlait Milk Limited supplies various dairy products to Synlait Foods (Talbot Forest) Limited, most notably raw milk.

In April 2020, Synlait Milk Limited acquired 100% of the share capital in Dairyworks Limited. Dairyworks Limited specialises in the processing, packaging, and marketing of dairy products, including cheese, butter, ice cream and milk powder. Synlait Foods (Talbot Forest) Limited supplies manufactured cheese products to Dairyworks Limited. Dairyworks Limited owns an Australian subsidiary, Dairyworks (Australia) Pty Limited.

Refer to Note 18 for further information on the acquisitions of both Synlait Foods (Talbot Forest) Limited and Dairyworks Limited which occurred in the year ended 31 July 2020

Key management and personnel compensation

Other than their salaries and bonus incentives, there are no other benefits paid or due to directors and executive officers as at 31 July 2020. The total short-term benefits paid to the key management and personnel is set out below.

	2020 $'000	2019 $'000
Short term benefits	6,398	5,773
Share based payments expenses (note 13)	523	644

20. RELATED PARTY TRANSACTIONS (CONTINUED)

(a) Other transactions with key management personnel or entities related to them

Information on transactions with key management personnel or entities related to them, other than compensation, are set out below.

(i) Loans to directors

There were no loans to directors issued during the period ended 31 July 2020 (2019: $nil).

(ii) Other transactions and balances

Directors of Synlait Milk Limited control 3.0% of the voting shares of the company at balance date (2019: 3.0%)

(b) Transactions with other related parties

	2020 $'000	2019 $'000
Purchase of goods and services		
Bright Dairy and Food Co Ltd - Directors fees	259	196
Sale of goods and services		
Bright Dairy and Food Co Ltd - Sale of milk powder products	4,074	6,464
Bright Dairy and Food Co Ltd - Reimbursement of costs	-	(91)
New Hope Innovation (Hong Kong) Trading Company Limited - Sale of milk powder products	1,773	-

(c) Outstanding balances

The following balances are outstanding at the reporting date in relation to transactions with related parties other than key management personnel:

	2020 $'000	2019 $'000
Current receivables (sales of goods and services)		
Bright Dairy and Food Co Ltd - Sale of milk powder products	-	1
Bright Dairy and Food Co Ltd - Reimbursement of costs	(492)	(233)
Sichuan New Hope Nutritionals Ltd - Sale of milk powder products	(71)	(72)
Sichuan New Hope Nutritionals Ltd - Other costs	292	296

21. CONTINGENCIES

The Group is currently involved in a dispute regarding restrictive covenants attached to land it purchased in Pokeno.

In February 2018, the Group announced the conditional purchase of 28 hectares of land in Pokeno to establish its second nutritional powder manufacturing site. The land was subject to restrictive covenants limiting the development of the land that the vendor was required to remove. The vendor applied to the High Court to have the restrictive covenants removed.

In November 2018, the High Court removed the restrictive covenants. The High Court also declined to award compensation to the covenant holder on the basis that they would not suffer any loss due to the extinguishment of the covenants as they were of little practical value. The Group took legal title to the land following the High Court's decision. The covenant holder appealed to the Court of Appeal which in May 2019 overturned the High Court's decision.

In June 2019, the Group filed an application for leave to appeal to the Supreme Court to have the Court of Appeal's decision overturned. The Supreme Court held an oral hearing on 21 October 2019 where leave to appeal was granted. The appeal was heard by the Supreme Court on 3 and 4 June 2020 and the Group is yet to receive the Court's ruling.

There are a range of possible outcomes for the Group including a negotiated settlement between the parties. Given the range of possible outcomes the Group is not able to reliably estimate any potential liability.

No other significant contingent liabilities are outstanding at balance date (2019: $nil).

22. COMMITMENTS

(a) Capital commitments

Capital expenditure contracted for at the end of the reporting period but not yet incurred is as follows:

	2020 $'000	2019 $'000
Pokeno processing plant	10,264	49,455
Liquid dairy packaging facility	1,188	16,916
Separator capacity upgrade	419	5,820
Dry Store 4	14,100	2,523
Pokeno Waste Water Initiative	571	-
Dunsandel farms (note 23)	25,700	-
Total	52,242	74,714

The above balances have been committed in relation to future expenditure on capital projects. Amounts already spent have been included as work in progress. There are no commitments to note for Synlait Foods (Talbot Forest) Limited and Dairyworks Limited.

(b) Operating lease commitments – group as lessee

Leases

The Group leases certain buildings, plant and equipment. Operating leases are where the lessor, rather than the Group, has effectively retained the substantial risk and benefit of ownership of a leased item. Operating lease payments are included in the determination of profit or loss in equal instalments over the period of the lease. Lease incentives received are recognised on a straight line basis over the lease period. From 1 August 2019, this policy only applies to short term and low value leases.

	2020 $'000	2019 $'000
Less than one year	167	3,468
Between one and five years	142	4,897
Greater than five years	-	537
Total	309	8,902

The operating leases relate to the leasing of warehouse and office space, vehicles and printers. All terms are reviewed on a regular basis. All leases are subject to potential renewal.

23. EVENTS OCCURRING AFTER THE REPORTING PERIOD

On 3 August 2020, Synlait Milk Limited incorporated a new subsidiary, Synlait Milk (Dunsandel Farms) Limited. The newly incorporated entity acquired two farms adjacent to the Group's Dunsandel facility for $25.7m on the same day. The Group received Overseas Investment Office approval to acquire the land on 24 February 2020.

There were no further events occurring subsequent to balance date which require adjustment to or disclosure in the financial statements.

24. OTHER ACCOUNTING POLICIES

Cash and cash equivalents

Cash and cash equivalents comprise cash balances, call deposits and cash held on trust by Tax Management New Zealand Ltd.

Goods and Services Tax (GST)

The profit and loss components of the statement of comprehensive income have been prepared so that all components are stated exclusive of GST. All items in the financial position are stated net of GST, with the exception of receivables and payables, which include GST invoiced.

Deloitte.

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF SYNLAIT MILK LIMITED

Opinion

We have audited the consolidated financial statements of Synlait Milk Limited and its subsidiaries (the 'Group'), which comprise the consolidated statement of financial position as at 31 July 2020, and the consolidated income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements, on pages 57 to 127, present fairly, in all material respects, the consolidated financial position of the Group as at 31 July 2020, and its consolidated financial performance and cash flows for the year then ended in accordance with New Zealand Equivalents to International Financial Reporting Standards ('NZ IFRS') and International Financial Reporting Standards ('IFRS').

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ('ISAs') and International Standards on Auditing (New Zealand) ('ISAs (NZ)'). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Company in accordance with Professional and Ethical Standard 1 International Code of Ethics for Assurance Practitioners (including International Independence Standards) (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' International Code of Ethics for Professional Accountants (including International Independence Standards), and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Other than in our capacity as auditor and the provision of other assurance and taxation compliance services, we have no relationship with or interests in the Company or any of its subsidiaries. These services have not impaired our independence as auditor of the Company and Group.

Audit materiality

We consider materiality primarily in terms of the magnitude of misstatement in the financial statements of the Group that in our judgement would make it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced (the 'quantitative' materiality). In addition, we also assess whether other matters that come to our attention during the audit would in our judgement change or influence the decisions of such a person (the 'qualitative' materiality). We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

We determined materiality for the Group financial statements as a whole to be $5,150,000.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

KEY AUDIT MATTER

Pōkeno Land Legal Dispute

In February 2018 the Group announced the conditional purchase of 28 hectares of land in Pōkeno to establish its second nutritional powder manufacturing site.

In November 2018, the High Court removed the covenants which would have hindered development of the land. The Group took legal title to the land following the High Court's decision.

In May 2019 the Court of Appeal overturned the High Court decision to remove the covenants.

In June 2019 leave was filed to appeal to the Supreme Court with an oral hearing occurring in October and the hearing taking place in June 2020.

The Group continues to be involved in legal proceedings and as at the date of this report there has been no ruling made by the Supreme Court.

The disclosure about and explanations of the legal dispute are contained in note 21 of the notes to the consolidated financial statements.

We have included the Pōkeno legal dispute as a key audit matter due to the level of judgement and uncertainty in relation to the legal dispute and the range of possible outcomes.

HOW OUR AUDIT ADDRESSED THE KEY AUDIT MATTER

We have evaluated the appropriateness of the accounting treatment, the assessment of the potential outcomes of the proceedings and the accounting presentation of the legal dispute by performing the following procedures:

- Reading the High Court and Court of Appeal judgements relating to the legal dispute;
- Discussing the matters with the Group's senior management including internal legal counsel;
- Obtaining and assessing the contents of a legal confirmation letter from the external counsel who are advising the Group on this matter; and
- Challenging management's assessment of the potential outcomes of proceedings and the appropriateness of treating the legal dispute as a contingent liability in accordance with NZ IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

We have found that the legal dispute has been appropriately disclosed as a contingent liability within note 21 to the notes to the consolidated financial statements.

KEY AUDIT MATTER

Acquisition Accounting

As detailed in note 18(b), Synlait Milk Limited acquired 100% of Dairyworks Limited ("Dairyworks") for a total consideration of NZD $112m on 1 April 2020. The acquisition resulted in the recognition of indefinite life intangible assets comprising brands of $15.8m and $43.4m of goodwill.

New Zealand accounting standards require the purchaser to identify the assets and liabilities acquired in a business combination, including identifiable intangible assets, and to measure them at fair value at the date of acquisition.

The Dairyworks brands has been valued using the relief from royalty method. The key assumptions applied in the model were:

- revenue growth rates;
- post-tax discount rate;
- royalty rate; and
- terminal growth rate.

We included the identification and valuation of intangible assets arising from the Dairyworks acquisition as a key audit matter because the Group's acquisitions are considered a key area of interest for investors and because of the size of this acquisition and the level of intangible assets. There is also significant judgement involved in identifying the intangible assets acquired and determining the appropriate methodology and key assumptions to calculate their fair value.

HOW OUR AUDIT ADDRESSED THE KEY AUDIT MATTER

We have evaluated the appropriateness of the accounting treatment for the intangible assets arising from the acquisition of Dairyworks, by performing the following procedures:

- Obtaining the sale and purchase agreement and related documents to corroborate the assets and liabilities acquired, focusing on the identification and measurement of intangible assets;
- utilising our knowledge to assess the Group's identification of intangible assets and consider what is represented by residual goodwill;
- comparing the forecast sales used in the valuation of the Dairyworks brands to approved forecasts; and
- challenging the reliability of the revenue growth rates by comparing the forecasts underlying the growth rates to historical forecasts and actual results of the underlying business.

We used our internal valuation specialists to assess the appropriateness of the nature and valuation of the intangible assets identified by the Group. This assessment included:

- evaluating the appropriateness of the valuation methodology and testing the mechanics of the model;
- evaluating the post-tax discount rate applied in the model through comparison to the cost of capital for the business and to external market data;
- and comparing the Group's assumed royalty rate to market data for similar intangible assets.

We have found that the identification and valuation of intangible assets arising from the Dairyworks acquisition have been appropriately accounted for in the consolidated financial statements.

Other information

The directors are responsible on behalf of the Group for the other information. The other information comprises the information in the Annual Report that accompanies the consolidated financial statements and the audit report. The Annual Report is expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

Our responsibility is to read the other information identified above when it becomes available and consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

Directors' responsibilities for the consolidated financial statements

The directors are responsible on behalf of the Group for the preparation and fair presentation of the consolidated financial statements in accordance with NZ IFRS and IFRS, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible on behalf of the Group for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs and ISAs (NZ) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

A further description of our responsibilities for the audit of the consolidated financial statements is located on the External Reporting Board's website at: https://www.xrb.govt.nz/standards-for-assurance-practitioners/auditors-responsibilities/audit-report-1

This description forms part of our auditor's report.

Restriction on use

This report is made solely to the Company's shareholders, as a body. Our audit has been undertaken so that we might state to the Company's shareholders those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company's shareholders as a body, for our audit work, for this report, or for the opinions we have formed.

Deloitte Limited

Andrew Dick, Partner
for Deloitte Limited
Auckland, New Zealand
25 September 2020

CORPORATE GOVERNANCE

Good corporate governance is top of mind for Synlait's Directors. It is a critical step in protecting the interests of our shareholders, customers, suppliers and other stakeholders. We strive to keep up to date with new developments, as appropriate for our business.

Synlait's shares are quoted on the NZX Main Board, and on the ASX. In December 2019 Synlait issued $180 million of subordinated bonds listed on the NZX Debt Market.

In this section, we report on the extent to which we followed the recommendations in the NZX Corporate Governance Code in the year to 31 July 2020. This section is current as at 31 July 2020 and has been approved by the Board.

Synlait acquired two operating subsidiaries in the year to 31 July 2020. A review will be undertaken in FY21 of their governance policies and procedures, including those addressed in the Corporate Governance Code. Where appropriate, Synlait's policies and procedures will be extended to those subsidiaries.

Synlait Dunsandel

PRINCIPLE 1: CODE OF ETHICAL BEHAVIOUR

'Directors should set high standards of ethical behaviour, model this behaviour and hold management accountable for these standards being followed throughout the organisation.'

Standards of Ethical Behaviour

Synlait's reputation matters to us. Synlait is committed to maintaining the highest standards of honesty, integrity and ethical conduct. Historically, this commitment has been embodied in our Code of Ethics and Synlait Standards Policy. These are complemented by our Whistleblower Policy, Securities Trading Policy, Continuous Disclosure Policy, Conflict of Interests Policy and Related Parties Transaction Policy. These policies outline in detail the expectations of people working with us. They include requirements to comply with all laws, as well as applicable internal rules, policies and procedures, deal fairly, not engage in bribery and corruption, and be circumspect with gifts, meals and entertainment. They also record that Synlait will not tolerate discrimination, bullying or harassment.

In July 2020 we consolidated our Code of Ethics and Synlait Standards Policy into one document, the new Synlait Standards Policy, which will be reviewed annually.

Our Whistleblower Policy supports the Synlait Standards Policy and the other associated policies. It is important that everyone at Synlait feels able to raise concerns about conduct. This policy gives those concerned about behaviour a process for raising those concerns, and assurance that their confidence will be protected where possible.

Breaches of the Synlait Standards Policy are treated seriously.

Securities Trading Policy

Synlait's Securities Trading Policy and Guidelines summarises the law on insider trading and Synlait's restrictions on Directors and employees dealing in Synlait's shares. The policy introduces a trading prohibition for Directors and certain employees at defined times ("blackout periods"). Outside the blackout periods, Directors and those employees are required to obtain consent before dealing in Synlait shares.

New Directors and employees receive information about this Policy when they commence with Synlait. Employees are also reminded about the Policy from time to time, including around the time of blackout periods.

PRINCIPLE 2: BOARD COMPOSITION AND PERFORMANCE

'To ensure an effective Board, there should be a balance of independence, skills, knowledge, experience and perspectives.'

Board Charter

Synlait's Board of Directors' Charter sets out the roles and responsibilities of the Board and its office holders, as well as other key information about the operation of the Board, including a requirement that the Board meets formally at least six times per year.

The Board delegates responsibility for implementing Synlait's strategic direction and managing Synlait's day-to-day operations to the Chief Executive Officer. This delegation is enacted in our Delegated Authorities Policy which all employees have access to. Management provides regular reports to the Board to assist the Board in meeting its responsibilities.

Nominations and appointment of Directors

Our Constitution, as approved by shareholders on 27 November 2019, includes our specific governance arrangements, including those relating to the makeup of our Board, and the Director appointment process. The Constitution relies on waivers from NZX Regulation granted on 27 November 2019 (in replacement for waivers granted before Synlait was listed). The full waivers are on our website and they are summarised from page 165.

The minimum number of Directors required to comprise Synlait's Board is three. The maximum number is eight. At least two Directors must be ordinarily resident in New Zealand. Currently, Synlait is required to have three independent Directors and a Managing Director of a Board Appointed Director. It currently has a Board Appointed Director, Dr John Penno. While it meets agreed shareholding thresholds, one of Synlait's shareholders, Bright Dairy Holding Limited (Bright Dairy), is entitled to appoint four directors, one of whom must be ordinarily resident in New Zealand and a Director of such standing and with such commercial and governance experience in New Zealand as is appropriate for a Director of an NZX listed company. That Director is the Hon. Ruth Richardson.

In preparation for Bill Roest's retirement at the Annual Meeting in 2020, and Graeme Milne's retirement in 2021, the People, Environment and Governance Committee has established a Nominations Sub-Committee. The Charter of the People, Environment and Governance Committee has been updated to include more detail around the Committee's roles and responsibilities in relation to nomination and appointment of Directors, and to outline the roles and responsibilities of the Sub-Committee.

The People, Environment and Governance Committee is responsible for making candidate recommendations to the Board. They use an external search company to assist them with this. In selecting candidates, they consider factors such as experience, qualifications, character, criminal record, bankruptcy history, judgment, the ability to work with other Directors, current Board composition and skill set, ability to fit with culture and independence. The principles of our Diversity and Inclusion Policy are also considered. Before any candidate is finally selected, appropriate fit and proper checks are undertaken. Important information about candidates will be provided to shareholders in the notice of the meeting at which they will vote on the appointment of a new Director.

Written agreements with Directors

It is important that all newly appointed Directors understand Synlait's expectations of them, and the entitlements that they will receive as a Director of Synlait. Synlait requires that all newly appointed Directors enter into agreements with Synlait outlining their terms of appointment. This agreement addresses matters such as time commitment required, standards to be met, remuneration arrangements, indemnity by Synlait, and insurance.

Disclosure of Information about Directors

Our current Board is shown on page 36 of this report and profiled on our website (https://www.synlait.com/people/). Other information about our Directors, including their remuneration, participation in Synlait securities and other interests is disclosed in the Statutory Information Section of this report starting on page 153.

Attendance at Board and Committee meetings in the year to 31 July 2020 was as follows:

Director	Board meetings attended	Audit and Risk Committee	People, Environment and Governance Committee
Bill Roest	10/10	4/4	4/4
Graeme Milne ONZM	10/10	4/4	4/4
Dr. John Penno	10/10		
Min Ben	7/10		2/4
Qikai Lu	10/10	2/4	
Hon. Ruth Richardson	10/10		4/4
Sam Knowles	9/10		4/4
Sihang Yang	10/10		

Diversity and Inclusion Policy

Synlait's Diversity and Inclusion Policy requires the Board to promote a culture of diversity and inclusiveness. It does by putting in place appropriate strategies and measurable objectives. Management must report to the Board on diversity initiatives and progress against the strategies and measurable objectives. The Board conducts an annual assessment of our Diversity and Inclusion Policy, our objectives set under that Policy, and the progress made towards achieving them.

We aim to achieve three main goals:

- Workforce Diversity – employ, develop and retain more women and Maori.
- Diversity through Leadership – empower and equip our people leaders to recruit, develop and retain a diverse and competent workforce.
- Workforce inclusion – foster a culture that encourages flexibility and fairness, to enable all employees to realise their potential, and thereby increase employee retention.

Our success will be measured against the following as at the end of 2023:

- Reduction of the gender pay gap to ≤ 5%;
- 40-50% of leadership positions (People Leaders, Supervisors, Specialist roles and Senior Leadership) held by women;
- No regretted losses of high potential female employees.

Mātua (our Parental Leave Policy) and Tāwariwari, (our Flexible Working Policy) assist us in meeting these goals. Since the introduction of these policies all our staff who have taken maternity leave have returned to work when expected.

We also offer un-conscious bias training and require regular reporting to the Board on candidate diversity.

In the year to 31 July 2020, our representation of women in leadership (People Leaders, Supervisors, Specialist roles and Senior Leadership) increased from 37% to 38% and the gender pay gap remained at 13%. We had no regretted losses of high potential female employees and continue to focus on attracting to Synlait the diverse talent pool we are looking to achieve.

Information collected in relation to the diversity of our Senior Leadership Team (comprising the Chief Executive Officer, his direct reports, and three additional managers who do not report to the Chief Executive Officer) as at 31 July 2020 is as follows (corresponding information for FY19 is in brackets):

Gender	Female	Male	Total	% Female
	3 (2)	9 (11)	12 (13)	25 (18)

Domicile	New Zealand	Other
(based on current residence)	12 (13)	0 (0)

Language spoken	English only	Two languages	Three or more
Senior Leadership Team	7 (9)	3 (1)	2 (3)

Director training

It is important that our Board stays up to date with market developments and has a good understanding of both Synlait's business and industry, and governance related matters. Each year our Board is involved in two strategy workshops with management to agree Synlait's vision and strategy. In addition, they spend a week together learning about various aspects of Synlait's business. In September 2019 the Board travelled to China to learn more about trading with China, and the infant, dairy and food service industries in China. They attended meetings with Bright Dairy, undertook market visits and participated in discussions focused on these areas.

New Directors will also participate in an induction programme, designed to educate them about Synlait, its business and its governance arrangements, so that they are well prepared for their role.

Assessment of Director, Board and Committee performance

Our Board Chair conducts an annual review of the Board and each Director, as required by our Board's Charter. The People, Environment and Governance Committee puts in place processes to assist with the review of the performance of the Board, and the performance of individual Directors, including that of the Chair and Committee Chairs, and the Board Appointed/Managing Director. An external review is conducted every three years.

Independent Directors

Three of our eight Directors are Independent. This meets the requirement in our Constitution for the number of independent directors (as permitted by waivers issued by NZX Regulation), but does not satisfy Recommendation 2.8 in the Corporate Governance Code which suggests that majority of our Board should be Independent. More information about the the makeup of our Board and the waivers issued by NZX Regulation can be found from page 165.

Synlait's Board Charter was updated this year and now includes more prescriptive requirements regarding Director independence. These include considerations such as previous employment by Synlait or its subsidiaries, provision of professional services to Synlait or its subsidiaries, business relationships with Synlait or its subsidiaries, relationship with substantial security holders, close personal ties, length of tenure and other interests.

Synlait has considered whether its Independent Directors are independent against the definition in the NZX Listing Rules, the commentary to Recommendation 2.4 in the Code, and its Board Charter and is satisfied that its Independent Directors are Independent. Their interests in shares in Synlait, and other relevant information is disclosed in the Statutory Information section of this report starting on page 153.

Chair of the Board

Synlait's Chair, Graeme Milne, is an Independent Director as required by our Constitution.

PRINCIPLE 3: BOARD COMMITTEES

'The board should use committees where this will enhance its effectiveness in key areas, while still retaining board responsibility.'

Synlait has two Board Committees: the Audit and Risk Committee and the People, Environment and Governance Committee (which now has the Nominations Sub-committee). These Committees undertake the operations described in their respective Charters. The Chair of each Committee reports back to the Board at each Board meeting, and makes recommendations, to the Board, when necessary. Synlait considers it has an adequate range of Committees for its size.

Audit and Risk Committee

Committee members: Bill Roest (Chair), Graeme Milne, Qikai Lu

The members of the Audit and Risk Committee are nominated by the Board, and most of their number, and the Chair, must be Independent Directors. At least one member of the Risk and Audit Committee must have accounting or related financial experience. The makeup of the Committee meets these requirements.

The Committee is chaired by Independent Director Bill Roest, who is a member of the Chartered Accountants Australia and New Zealand and a fellow of the Association of Chartered Certified Accountants (UK). Bill will step down from our Board, and therefore the Audit and Risk Committee, at this year's Annual Meeting. Qikai Lu has considerable financial and business experience and has previously been a public accountant with one of the 'big four' chartered accounting firms in China.

This Committee ensures that the Board is aware of matters that may significantly affect the financial condition or affairs of Synlait's business, and it prepares any reports required by law, regulation or the NZX Listing Rules or requested by the Board. It reviews the interim financial statements, annual financial statements and preliminary announcements before their release. It oversees risk management at Synlait, legislative and other compliance (including with internal policies), tax management, treasury management and sales management. Its role with respect to Synlait's auditors, both external and internal, is discussed on page 149.

As required by its Charter, the Committee reviews its performance against its Charter, and the Charter itself, at least once per year.

The Chief Executive Officer, Chief Financial Officer, Director Legal, Risk and Governance and Company Secretary have a standing invitation to attend meetings of this Committee. Other members of Synlait's management team may attend on specific invitation only.

People, Environment and Governance Committee

Committee Members: Sam Knowles (Chair), Graeme Milne, the Hon. Ruth Richardson, Bill Roest and Min Ben

The People, Environment and Governance Committee performs key human resources (including remuneration), governance and sustainability tasks for the Board. The majority of the Committee's members must be Independent, and the Board appoints the Chair of the Committee. At least one of the Committee's members must have experience with a listed company. The composition of the Committee meets these requirements.

In 2020, the People, Environment and Governance Committee established its Nominations Sub-committee to assist with preparations for the nomination and/or appointment of new Directors. The role of the Sub-committee is described in more detail in the Charter of the People, Environment and Governance Committee. Independent Directors Graeme Milne and Sam Knowles are the members of the Sub-committee.

The Chief Executive Officer, Director, People, Culture and Performance, Director, Legal, Risk and Governance, Director, Sustainability and Brand and Company Secretary have a standing invitation to attend meetings of this Committee. Other members of Synlait's management team may attend on specific invitation only.

Takeover Protocols

Synlait has a Takeovers Policy setting out the procedure to be followed if there is a takeover offer for Synlait. That Policy records that the Board may establish an Independent Takeover Committee, including Synlait's Independent Directors, to manage the process.

PRINCIPLE 4: REPORTING AND DISCLOSURE

'The Board should demand integrity in financial and non-financial reporting, and in the timeliness and balance of corporate disclosures.'

As a result of its listings on the NZX and the ASX, Synlait is required to comply with strict reporting and disclosure requirements to keep its shareholders, customers and other stakeholders informed as to its activities.

Continuous Disclosure

Our Continuous Disclosure Policy assists staff to comply with the strict reporting and disclosure requirements imposed on Synlait as a listed company. All staff are required to be familiar with Continuous Disclosure Policy and associated procedures so that they can identify a potential need for disclosure. All Directors and members of Synlait's Senior Leadership Team are primarily responsible for compliance with the disclosure obligations and implementing the Policy effectively.

Documents available on Synlait's website

Synlait publishes its key Charters, Policies and Standards, including those referred to in this report and other key documents, on its website.

Financial reporting

At each Board meeting our full Board is presented with a detailed Business Performance Report (BPR), which considers our financial performance. It identifies any risks, issues and opportunities, and attempts to quantify the upsides and downsides should any of these eventuate. The BPR also measures forecasts against actual performance and explains the reasons for any variances – including whether these are timing differences or permanent variances.

Synlait is committed to ensuring the integrity and timeliness in its financial reporting, and to providing information to shareholders in a timely manner. The Board has a rigorous process to ensure the quality and integrity of our financial statements.

The Audit and Risk Committee oversees external financial reporting, including the accuracy and timeliness of financial statements. It is charged with reviewing in significant detail the financial statements and accompanying materials. After approval by the Audit and Risk Committee, the complete set of financial statements and related report is submitted to the full Board for approval.

Management makes detailed representations to the Board to assist them in their consideration of the draft financial statements. Each Director is obliged to form a view on the quality, accuracy and integrity of the financial statements and annual report and give their approval (or not) in accordance with the Financial Markets Conduct Act 2013 and Companies Act 1993.

Care is taken to ensure that all reporting to investors is accurate, balanced and clear. Synlait's full and half year financial statements were prepared in accordance with relevant financial standards. The full year financial statements are set out on pages 57 - 127 of this report.

On our website, we have our previous years' financial statements, investor presentations and analyst briefings available for our shareholders.

Non-financial disclosure

Our annual report has traditionally been focused on reporting against financial measures. In FY19, we established our sustainability framework and related Sustainable Innovation Platforms (SIPs) which align to our purpose and strategy. We also established baseline information in relation to some of our goals. We intend to publish a separate sustainability report in November 2020.

PRINCIPLE 5 - REMUNERATION

'The remuneration of directors and executives should be transparent, fair and reasonable.'

Director remuneration

The People, Environment and Governance Committee is responsible for reviewing the structure of Directors' remuneration. It obtains independent advice on appropriate remuneration and recommends to the Board the remuneration to be proposed for shareholder approval at the annual meeting. The independent advice considers the remuneration paid to Directors of similar companies to Synlait.

Current Directors' remuneration is set out in the statutory information section of this report on pages 159 - 160, and was approved by shareholders on 27 November 2019. The Director remuneration report prepared by Ernst & Young in September 2019 for shareholder consideration is on our website.

Remuneration Policy

The principles applying to remuneration of our Directors and employees are set out in our Strategic Remuneration Policy. They are designed to ensure that Synlait meets the strategic policy objective of attracting, rewarding and retaining staff with the requisite skills and capabilities to ensure our successful business outcomes.

The People, Environment and Governance Committee oversees the implementation of our Strategic Remuneration Policy, including recommending to the Board remuneration for the CEO and other business leaders, and budget parameters for the annual pay review.

Director remuneration is paid by way of Director Fees. Employee fixed remuneration comprises a base salary, employer KiwiSaver contributions (for participating employees), and medical insurance. Remuneration is reviewed yearly for eligible employees, with any changes based on market movement, position in the salary range, and performance.

Synlait does not offer bonuses or other short-term incentives. It operates a Long-Term Incentive Scheme (LTI Scheme) which a small group of selected senior employees are invited to join each year. Any benefits from the LTI Scheme are in addition to the salary and other benefits agreed with the participating employee.

The LTI scheme is an annual scheme with Performance Share Rights (PSRs) granted to Board-approved participants in July in each year it operates. PSRs are non-transferable and have no voting or other share rights and are otherwise subject to the rules of the LTI Scheme and individual award agreements.

Each PSR will be converted into one ordinary share in Synlait after the Board determines that specified performance hurdles have been met during the assessment period of three financial years following the date of the grant. This is provided however that the employee remains employed by Synlait at the end of the assessment period. No cash consideration is payable by the employee on the grant of PSRs, or on the issue of fully paid ordinary shares following vesting of PSRs.

The LTI Scheme requires two performance hurdles to be met, relating to total shareholder return (TSR) and earnings per share (EPS). Vesting of half of the total award is dependent on the TSR target being met, and the remaining half, the EPS target being met. The degree of vesting in each case is determined by a progressive vesting scale. If our TSR is greater than or equal to the 75th percentile of a peer group over the assessment period, a minimum of 50% of the PSRs will vest. The peer group comprises the S&P/NZX 50 index companies on the first day of the assessment period. If our EPS over the assessment period equals the Board approved EPS target plus 10%, then a minimum of 50% of the PSR will vest. For either performance hurdle to be met, our TSR must be positive over the assessment period.

In 2019, Synlait issued 83,880 shares to senior employees under the 2017 LTI Scheme. Vesting of annual awards is monitored to ensure that the value vested in any one year does not exceed 5% of market capitalisation, as required by NZX Listing Rules.

There are currently 334,880 PSRs on issue. The PSRs have been issued under the 2018, 2019 and 2020 LTI Schemes, and may vest as contemplated by the terms of the LTI Scheme, in each case based on Synlait's performance over the previous three financial years.

Chief Executive Officer Remuneration

In the year to 31 July 2020, Leon Clement's remuneration comprised of a base salary of $915,236, a 3% employer KiwiSaver contribution, and medical insurance. Leon was also awarded 23,372 PSRs as a part of Synlait's FY20 LTI Scheme. Those PSRs had a value as at 31 July 2020 of $162,903, on the assumption that all PSRs convert to shares after 31 July 2022.

PRINCIPLE 6 - RISK MANAGEMENT

'Directors should have a sound understanding of the material risks faced by the issuer and how to manage them. The Board should regularly verify that the issuer has appropriate processes that identify and manage potential and material risks.'

Synlait's risk management framework and risks

Synlait's risk management framework is aligned to ISO31000:2018 guidelines. Synlait operates under a Risk Management Policy, with supporting standards and procedures to achieve a consistent approach. The Board has approved the Policy, which documents Synlait's healthy strategic risk appetite. Four principles are recognised in the Policy as guiding all risk-related activities and decision making:

- Nothing we do is worth getting hurt for;
- We do not accept activities, behaviour or decisions which create uncontrolled risk to the consumers of our products;
- We do not accept activities, behaviour or decisions which knowingly constitute a legal or regulatory breach;
- We do not accept uncontrolled risks that could result in a significant loss of revenue, profitability and/or earnings.

Several other policies and procedures are in place to support active management of key operational risks. These include a Delegated Authorities Policy, Tax Risk Management Policy, Health Safety and Wellbeing Policy and Food Safety and Quality Policy.

The Audit and Risk Committee is responsible for ensuring management:

- Has processes for identifying, assessing and responding to strategic and operational risks;
- Is promoting an appropriate "control culture" throughout the business, with supporting processes and systems in place.
- Is regularly reviewing and evaluating the effectiveness of these processes, and implementing improvements identified.

The Committee reviews Synlait's risk profile at each meeting, along with progress on mitigations and material changes. A summary of the profile and changes is provided to the Board at each meeting.

At Synlait, risk is everyone's responsibility. This principle is supported by an integration of risk management processes within key business functions and activities including:

- Integrated Business Planning (IBP), with formal risk review processes built-in throughout each cycle.
- Project Management Office (PMO), with detailed risk assessment and management processes embedded at all levels.
- Health, Safety and Wellbeing, including a thorough permit to work process and critical risk programme.

Synlait's enterprise risk management framework is applied across all sites and operations, including those of subsidiaries. Existing risk management processes with new subsidiaries, Dairyworks Limited and Synlait Foods (Talbot Forest) Limited, are being aligned to the Synlait framework, with material risks affecting those businesses forming part of management reporting to the Audit and Risk Committee and Board.

To ensure consistency and appropriate focus, Synlait assesses risks as either:

- Strategic – that is, risks faced by Synlait because of the strategic objectives and/or decisions taken; or
- Operational – that is, risks faced in in the pursuit of delivering on the objectives.

This table below summarises material risks currently being monitored by the Board and management.

Risk type	Short description	Mitigation
Strategic	Market access	Our Regulatory and Corporate Affairs teams proactively manage this risk through: • Regular scanning of the regulatory environment for trends, changes and areas of potential risk for Synlait. • Maintaining strong relationships with local and international networks to calibrate or strengthen our understanding of potential changes and their impact; • Regular engagement with key New Zealand international industry groups - including Dairy Companies Association of New Zealand, DairyNZ and the Infant Nutrition Council - to promote the interests of Synlait and New Zealand dairy; and • Regular and meaningful engagement with relevant • Ministers, officials and advisors to build understanding of Synlait's business, our interests and shared commitments.
	Delivering on sustainability	• Synlait is committed to enhancing its sustainability reporting. As part of our Sustainability Framework, eleven Sustainable Innovation Platforms (SIPs) have been identified. • Within each of these, detailed targets and implementation plans are developed and closely tracked by management, with regular reporting to the Board via the People, Environment and Governance Committee.
	Consumer substitution	• Active monitoring of changes in the global nutrition market across multiple functions including category management, research and development, technical and regulatory. • Regular engagement in market research and analysis to understand consumer and/or market preferences.
	Maintaining agile culture	• Synlait Way of Working has been developed to support agile and flexible culture. This was operationalised prior to COVID-19 and has been further refined as part of the COVID review process. • Regular employee engagement surveys and planning processes to ensure teams make tangible progress on key drivers of engagement.

Risk type	Short description	Mitigation
Operational	Major site or supply chain disruption	• Business continuity plans in place at all operational sites. • Service level agreements in place with key providers and partners.
	Major health and safety event	As described on page 148.
	Major food safety / quality event	Comprehensive quality management system in place which includes: • Strict operational controls throughout the value chain; • Thorough testing programmes, including raw milk, ingredients, finished product and across processing environment; • Training for all staff commensurate to their position; and • Regular internal and external audits to verify controls and drive a focus on continuous improvement.
	Technology compromise	• Cyber security programme of work commenced in FY20 to lift capability to prevent, prepare for and respond to disruptive events. • Contingencies and disaster recovery plans in place to mitigate impacts of disruption.
	Major compliance breach	Compliance programme in place, currently under refresh (to be completed early FY21). Monitoring and regular reporting of compliance obligations and performance against these.
	Talent management	• Continued development of the Future Leaders programme, which aims to attract and develop leaders in line with purpose, ambition and strategy; • Investment in best-in-class systems to support a highly effective talent acquisition process; • Comprehensive workforce planning and talent review processes embedded in regular management reviews; and • Continued refinement of the Perform and Grow framework, ensuring every employee is engaged in regular development activities.
	System and process maturity	Investment in an enterprise resource planning (ERP) system to enhance core operational systems.

Health and Safety Risks

Synlait measures proactive and reactive measures of health, safety and wellness (HSW). These include our Total Recordable Injury Frequency Rate (TRIFR), Near Miss and New Hazard frequency rates, and Injury Severity frequency rate.

Over the course of FY20, Synlait's TRIFR decreased from 13.7 to 7.6. The target was 9.0.[1]

Synlait has identified five critical health and safety risks in its business. They are hazardous gases, working at heights, material handling equipment, working in confined spaces and State Highway One (traffic). We have projects actively seeking to reduce the likelihood and consequence of an event linked to those critical risks being fatal or seriously harming any person (employee or contractors).

As part of our strategy to reduce the likelihood of an ammonia leak, and the impact of any leak, we have recently completed an external ammonia safety assessment. The ammonia safety assessment provided us with assurance our current system is of a high standard.

In FY20 we implemented 45 engineering controls to reduce the risk of falls. This was a shortfall of 19 against our FY20 target, as a result of the COVID-19 restrictions. We intend to complete a further 105 in FY21.

The business has strengthened its focus on quality real time health and safety training that is specific to the needs of individual employees. We have selected two core providers to deliver tailored health and safety training that, at minimum, meets the New Zealand unit standards. One of the key factors of the success of this training is that it is delivered on site with our people.

We have deployed a permit to work system at Synlait Pokeno, to assess and control the risk of work undertaken on our sites, ranging from simple painting jobs to high risk activities involving confined spaces, heights and cranes. We had intended to have the same system in place at Synlait Dunsandel by the end of FY20, however COVID-19 restrictions delayed the implementation of this.

In FY20, an internal audit was completed on the occupational health and safety management systems at Synlait, based on ISO45001, an international standard that provides a framework to support organisation in the identification of health and safety risks. The internal audit has provided the business with the ability to identify some process and procedures improvements to ensure that our health and safety framework is robust, yet flexible enough to adapt with the business.

More information on Synlait's health and safety initiatives will be included in our Sustainability Report published later this year.

[1]Health and Safety is managed separately at operating subsidiaries.

PRINCIPLE 7 – AUDITORS

'The board should ensure the quality and independence of the external audit process'.

External Auditors

The Audit and Risk Committee plays a key role in Synlait's audit process. It is responsible for recommending the appointment of the external auditors to the Board, overseeing the independence and the work of the external auditors; as well as reviewing policies for the provision of non-audit services by the external auditor (including the framework for pre-approval of any such services).

Currently, Deloitte is the Synlait group's external auditor. A representative from Deloitte attends our Annual Meeting of Shareholders where the lead audit partner is available to answer questions from shareholders.

The Audit and Risk Committee meets regularly with Deloitte, (including meeting without management present). Annually, the Audit and Risk Committee reviews and assesses Deloitte's performance through an internal questionnaire. The results, key themes and recommendations are reported to the Board.

Deloitte confirms their independence from the Company to the Audit and Risk Committee in March and September each year. Non-audit services performed by Deloitte are closely examined by management and the Chair of the Audit and Risk Committee prior to engaging Deloitte for these additional services, to ensure that they do not compromise Deloitte's independence.

In the year to 31 July 2020, our total payments to Deloitte were as follows:

Audit and Assurance Work	$463,115
Taxation Compliance and accounting advice[1]	$52,917
Percentage non-audit	10%
Percentage audit	90%

[1] Various engagements for members of the Group including income tax return review, GST review, FBT reviews, high-level review of tax governance processes, subsidiary onboarding, and ad hoc review work. These services are compliance in nature and are not inconsistent with Deloitte's role as auditor. Deloitte's ongoing role as provider of tax compliance services was approved by the Audit and Risk Committee.

Internal audit

Synlait has a Senior Internal Auditor who performs key risk and business process focused internal audit reviews across Synlait's operations. These are undertaken as part of an annual programme of work agreed with the Audit and Risk Committee. The Audit and Risk Committee is responsible for reviewing the activities, resources and organisational structure of the internal audit function. In due course, internal audits will extend to Synlait's operating subsidiaries, as determined appropriate by the Audit and Risk Committee.

PRINCIPLE 8 - SHAREHOLDER RIGHTS AND RELATIONS

'The Board should respect the rights of shareholders and foster relationships with shareholders that encourage them to engage with the issuer.'

It is important that we communicate with our shareholders to keep them informed. It is equally important that they can communicate with us and exercise their shareholder voice.

Website

We aim to ensure investors understand all our activities by communicating regularly with them, using clear and balanced information. Our website is just one of our key information channels, which include NZX and ASX websites (announcements), and:

- Our website, including its investor and news sections: synlait.com;
- Our social media channels (LinkedIn and Facebook);
- Our annual report;
- Our interim update; and
- Our annual meeting.

The investor section of Synlait's website contains the below information:

- A live share price feed (from the NZX and ASX), historical pricing and trading data;
- Announcements and news releases, copies of previous annual and interim reports and investor presentations;
- Recordings and transcripts from results calls;
- Key corporate governance documents such as Charters and Policies, including Synlait's constitution;
- Notices of Meeting, results of meetings and other relevant meeting materials;
- Key dates in the investor schedule, such as annual meeting, full and interim reporting dates; and
- Share registry information.

Communicating with Synlait

Instructions on how to reach the investor relations team and company secretary are available on our website. We aim to respond to all shareholder communications in a timely manner.

Shareholders can elect to receive Synlait communications in the manner which suits them best – either electronically or via mail. Through our share registry, Computershare, shareholders can amend their communication preferences at any time.

Right to vote

Synlait's constitution and the NZX Listing Rules afford shareholders the right to vote on certain matters affecting Synlait. Our shareholders can vote at any meeting of shareholders in person or by using a representative. On a vote by show of hands, each shareholder attending in person or by their representative has one vote. If a poll is taken, each shareholder attending in person or by their representative has one vote per fully paid up share they hold. Postal votes are not permitted unless the Board notifies shareholders otherwise. More information on voting is in our constitution on our website.

Notice of annual meeting

Synlait's last annual meeting was held on Wednesday 27 November 2019. The Notice of Meeting was released to the market on 29 October 2018. An audio recording of the meeting is available in the investor centre on the company's website.

Our 2020 meeting will be held on Wednesday 25 November. A Notice of Meeting will be issued in October. A webcast of the meeting will be made available to shareholders after the meeting.

STATUTORY INFORMATION

01. BUSINESS OPERATIONS

Synlait is a milk nutrition company. We combine expert farming with state-of-the-art processing to produce a range of nutritional milk products. A full summary of our business model and how we create value is on pages 22 - 23.

In the year to 31 July 2020, we completed two acquisitions in delivering on our diversification strategy:

- The purchase of the business and selected assets of Talbot Forest Cheese on 1 August 2019. This is owned and operated by our subsidiary, Synlait Foods (Talbot Forest) Limited; and
- The purchase of the shares in Dairyworks Limited on 1 April 2020. Dairyworks Limited specialises in the processing, packaging and marketing of cheese, butter, milk powder and ice cream.

Commissioning of our infant capable powder manufacturing facility at Synlait Pokeno was completed during the year. Synlait Pokeno enables us to grow and reduce our risk profile, through the diversification of processing facilities and milk pools beyond Synlait Dunsandel.

On 3 August 2020, we acquired farmland adjacent to our Dunsandel facility. This acquisition enables us to pursue several strategic supply chain and sustainability initiatives that will support Synlait Dunsandel's long-term operation and expansion.

Synlait Dunsandel, Canterbury

02. DIRECTORS

Synlait's Directors are profiled on our website, https://www.synlait.com/people/. This table sets out the directors of the Synlait group companies as at 31 July 2020, with changes following the balance date also noted:

Company	Directors	Appointment	Appointed
Synlait Milk Limited Synlait Milk Finance Limited	Graeme Milne ONZM (Chair)	Independent	23 March 2006
	Bill Roest	Independent	8 May 2013
	Dr John Penno	Board Appointed	21 July 2013[1]
	Min Ben	Bright Dairy Appointed	29 November 2016
	Qikai Lu	Bright Dairy Appointed	8 December 2015
	Hon. Ruth Richardson	Bright Dairy Appointed	16 November 2009[2]
	Sam Knowles	Independent	4 July 2013
	Sihang Yang	Bright Dairy Appointed	11 November 2010

Company	Directors
The New Zealand Dairy Company Limited	Graeme Milne ONZM (Chair) Nigel Greenwood until 24 June 2020
Eighty Nine Richard Pearse Drive Limited	Graeme Milne Nigel Greenwood until 24 June 2020
Synlait Business Consulting (Shanghai) Co., Limited	Deborah Marris Martijn Jager Nigel Greenwood until 10 June 2020 Boyd Williams from 10 June 2020
Synlait Foods (Talbot Forest) Limited	Leon Clement Nigel Greenwood until 24 June 2020
Dairyworks Limited[3]	Dr John Penno (Chair) from 1 April 2020 Graeme Milne from 1 April 2020 Leon Clement from 1 April 2020 Sam Knowles from 1 April 2020 Paul Brown until 1 April 2020 Margaret Cross until 1 April 2020 Peter Cross until 1 April 2020 Stuart Gray until 1 April 2020
Dairyworks Australia (Pty) Limited	Craig Stevens Peter Cross until 1 April 2020

[1] Prior to this, John had been a Director of Synlait Limited, which has since been removed from the Register of Companies. When first appointed to the Board of Synlait Milk Limited, John was CEO and Managing Director. In November 2018, following stepping down as CEO, he became the Board Appointed Director.

[2] When first appointed to Synlait Milk Limited, Ruth was an Independent Director. In 2013, she became a Bright Dairy appointed Director.

[3] The Board of Dairyworks Limited changed on the purchase by Synlait of all of the shares in Dairyworks Limited on 1 April 2020.

03. DIRECTOR INTERESTS

The following declarations of interest were made by Directors of Synlait and its subsidiaries under section 140(2) of the Companies Act 1993 during the year to 31 July 2020:

Graeme Roderick Milne
Chairman Synlait Milk Limited
Chairman Pro-Form Limited Advisory Board until 28 February 2020
Director Synlait Milk Finance Limited
Director Eighty Nine Richard Pearse Drive
Director The New Zealand Dairy Company Limited
Director of Dairyworks Limited from 1 April 2020
Chairman Terracare Fertilisers Limited
Director Alliance Group Limited
Director Elviti Holdings Limited
Director NZP Holdings Limited
Director New Zealand Pharmaceuticals Limited
Director of Elviti Finance Limited
Director of Nyriad Limited
Director of Nyriad Nominee Limited
Chairman of PF Olsen Limited
Director PF Olsen Group Ltd
Chairman of Advisory Board Rimanui Farms Limited
Council member Waikato University
Member of Zespri Director Remuneration Committee from 1 October 2019
Trustee Rockhaven Trust
Partner GR & JA Milne
Shareholder in Synlait Milk Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Ruth Margaret Richardson
Chair Kula Fund Advisory Committee until 31 December 2019
Chair SYFT Technologies Limited until 20 August 2019
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Director Ruth Richardson (NZ) Limited
Chair New Zealand Merino Company Limited
Director Bank of China (NZ) Limited
Shareholder in Synlait Milk Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Willem Jan (Bill) Roest
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Director Housing Foundation Limited
Director Metro Performance Glass Limited until 30 June 2020
Independent Chair of Fisher & Paykel Appliances Limited Audit Committee until 31 March 2020
Trustee New Zealand Housing Foundation
Trustee WJ & IJ Family Trust
Shareholder in Synlait Milk Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Qikai Lu
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Director Ba'emek Advanced Technologies Limited until 24 February 2020
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Min Ben
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Sihang Yang
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

John William Penno
Board Appointed Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Chairman Dairyworks Limited from 1 April 2020
Director Sichuan New Hope Nutritional Foods Co., Limited (awaiting confirmation of registration of resignation)
Director Okuora Holdings Limited
Director The Pure Food Co Limited
Director Leaft Foods Limited
Director Thorndale Dairies Limited
Trustee John Penno Trust
Shareholder in Okuora Holdings Limited (and through Okuora Holdings Limited, Pastoral Robotics Limited, Signum Holdings Limited and The Pure Food Co Limited)
Shareholder Leaft Foods Limited
Shareholder in Thorndale Dairies Limited
Shareholder in Synlait Milk Limited
Shareholder in The Pure Food Co Limited
Chair of Fresh Water Leaders Group reporting to Ministers Parker and O'Connor
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Ian Samuel (Sam) Knowles
Director Synlait Milk Limited
Director Synlait Milk Finance Limited
Director of Dairyworks Limited from 1 April 2020
Director Trustpower Limited until 24 July 2020
Director Rangatira Limited
Director Fire Security Services 2016 Limited
Director Umajin Limited
Chairman OnBrand Limited
Chairman Adminis Limited
Director Magritek Limited
Director Com Investments Limited
Director Growthcom Limited
Director Habourside Rentals Limited
Director of Montoux Limited
Trustee Te Omanga Hospice Foundation
Trustee Ruby Family Trust
Trustee WWF NZ
Trustee Com Trust
Trustee Ian Samuel Knowles Children's Trust
Shareholder in Synlait Milk Limited
Receipt of Directors' Fees from Synlait Milk Limited at approved rate
Insurance cover arranged by Synlait Milk Limited
Deed of Indemnity and Access from Synlait Milk Limited

Leon Clement
Director Synlait Foods (Talbot Forest) Limited
Director of Dairyworks Limited from 1 April 2020
Director POD Farming Limited
Shareholder POD Farming Limited
Insurance cover arranged by Synlait Milk Limited

Nigel Greenwood (Appointment as CFO ended in June 2020)
Director Eighty Nine Richard Pearse Drive until 24 June
Director The New Zealand Dairy Company Limited until 24 June 2020
Director Synlait Foods (Talbot Forest) Limited until 24 June 2020
Director Synlait Business Consulting (Shanghai) Co; Limited until 10 June 2020
Insurance cover arranged by Synlait Milk Limited

Paul Brown (previously a Director of Dairyworks Limited untl 1 April 2020)
Director P.G. Brown Holdings Limited
Director Moortool Limited
Director ICE Interiors Limited
Director Walbro Limited
Director Kawerau Dairy General Partner Limited
Independent Chair H.G. Leach and Company Limited
Independent Director Leach and Co Limited
Shareholder P.G. Brown Holdings Limited
Shareholder Moortool Limited
Shareholder ICE Interiors Limited
Shareholder Walbro Limited

Stuart Gray (previously a Director of Dairyworks Limited untl 1 April 2020)
Director Isfahan Limited
Shareholder Isfahan Limited
Shareholder Okaihau Pastoral Holdings Limited, indirectly through Isfahan Limited

Margaret Cross (previously a Director of Dairyworks Limited untl 1 April 2020)
Director Iron Holdings Limited
Director Opulence Hair Limited
Shareholder Iron Holdings Limited
Shareholder Opulence Hair Limited

Peter Cross (previously a Director of Dairyworks Limited untl 1 April 2020)
Shareholder Iron Holdings Limited

No Director requested to disclose or use information in their possession as a Director of Synlait or its subsidiaries that would not otherwise have been available to him or her.

As permitted by section 162 of the Companies Act 1993 and our Constitution, Synlait indemnifies and insures Directors and Officers against liability to other parties that may arise in the course of their activities as a Director or Officer. Details of the indemnities and insurance are kept in Synlait's Interests Register. This cover does not apply to any liabilities arising from criminal or reckless acts by our Directors or Officers.

04. DIRECTOR REMUNERATION

The annual fees paid to Directors of Synlait, as approved by shareholders on 27 November 2019 and effective 1 April 2020, are:

Directors, excluding the Chair and Committee Chairs	$88,900
Board Chair	$178,000
Audit and Risk Committee Chair	$104,150
People Environment and Governance Committee Chair	$100,900

This table sets out total remuneration and the value of other benefits received by Synlait Directors during the year ended 31 July 2020, being a combination of fees approved by shareholders at the last two annual meetings.

Directors	Role	Remuneration
Graeme Milne ONZM	Director, Board Chair	$172,000
Bill Roest	Director Audit and Risk Committee Chair	$99,383
Dr John Penno	Director	$86,300
Min Ben	Director	$86,300
Qikai Lu	Director	$86,300
Hon. Ruth Richardson	Director	$86,300
Sam Knowles	Director People, Environment and Governance Committee Chair	$98,300
Sihang Yang	Director	$86,300
Total		**$801,183**

Fees are not paid to Directors or employees of Synlait for acting as a Director of any Synlait subsidiaries.

Prior to the purchase by Synlait of the shares in Dairyworks Limited, fees and other benefits were paid to the directors of Dairyworks Limited in the year to 31 July 2020 as follows:

Directors	Remuneration
Paul Brown	$40,000
Stuart Gray	$22,666
Margaret Cross	$26,066

05. DIRECTOR HOLDINGS

This table sets out the relevant interests held by Synlait Directors in securities issued by Synlait:

Directors	Securities held (legally or beneficially) as at 31 July 2020	Securities held (legally or beneficially) as at 31 July 2019
Graeme Milne ONZM	72,753 ordinary shares	72,753 ordinary shares
Bill Roest	27,750 ordinary shares	27,750 ordinary shares
Dr John Penno	5,100,000 ordinary shares	5,100,000 ordinary shares
Min Ben	0	0
Qikai Lu	0	0
Hon. Ruth Richardson	56,222 ordinary shares	56,222 ordinary shares
Sam Knowles	55,000 ordinary shares	55,000 ordinary shares
Sihang Yang	0	0

06. EMPLOYEE REMUNERATION

During the year ended 31 July 2020, 316 employees (including former employees) of Synlait and its subsidiaries (not being Directors) received remuneration and other benefits, in their capacity as employees, of $100,000 or more, as set out below:

Salary bracket ($)	Number of employees
100,000 - 109,999	58
110,000 - 119,999	71
120,000 - 129,999	46
130,000 - 139,999	20
140,000 - 149,999	27
150,000 - 159,999	16
160,000 - 169,999	7
170,000 - 179,999	12
180,000 - 189,999	11
190,000 - 199,999	8
200,000 - 209,999	9
210,000 - 219,999	8
220,000 - 229,999	1
230,000 - 239,999	2
240,000 - 249,999	1
250,000 - 259,999	2
260,000 - 279,999	1
290,000 - 299,999	1
320,000 - 329,999	1
330,000 - 339,999	1
340,000 - 349,999	1
360,000 - 369,999	1
380,000 - 389,999	2
400,000 - 409,999	1
420,000 - 429,999	1
450,000 - 459,999	1
490,000 - 499,999	1
510,000 - 519,999	2
640,000 - 649,999	2
910,000 - 919,999	1
Total	316

These figures also include the value of shares issued to employees under the 2017 LTI Scheme during the year to 31 July 2020.

Synlait's Strategic Remuneration Policy is approved by Synlait's People, Environment and Governance Committee. That Committee also reviews and recommends to the Board the remuneration of the Chief Executive Officer and the Executive Leadership Team.

07. DONATIONS

Synlait made no donations in the year to 31 July 2020. Dairyworks Limited, a subsidiary of Synlait from 1 April 2020, made cheese donations to a value of $5,900 in the year ended 31 July 2020.

08. AUDITORS

Information about Synlait's auditor and its audit process, including audit and other fees paid to the auditor, is on pages 149.

09. STOCK EXCHANGE LISTINGS

Synlait's ordinary shares have been listed on the NZX Main Board since 23 July 2013 (ticker code: SML).

On 24 November 2016 Synlait completed a compliance listing on the ASX as a foreign exempt issuer (ticker code: SM1). As an ASX foreign exempt issuer, Synlait must comply with the NZX Listing Rules (other than as waived by NZX Regulation) and is exempt from complying with most of the ASX Listing Rules, as set out in ASX Listing Rule 1.15.

In December 2019, Synlait issued $180 million of unsecured, subordinated, fixed rate bonds with an interest rate of 3.83% per annum. These securities are quoted and trade on the NZX Debt Market (ticker code: SML010).

10. TOP 20 SECURITY HOLDERS AND SUBSTANTIAL SECURITY HOLDERS

Synlait had the following securities on issue as at 31 July 2020:

- 179,306,908 ordinary shares
- 180,000,000 subordinated bonds.

Set out below are Synlait's 20 largest shareholders as at 31 July 2020:

	Number of shares held	Percentage of ordinary shares
01. Bright Dairy Holding Limited	69,968,944	39.0%
02. The a2 Milk Company (NZ) Limited	35,574,646	19.8%
03. FIL Group Limited[1]	9,592,598	5.3%
04. John Penno	5,100,000	2.8%
05. ECP Asset Management Pty Ltd	3,027,486	1.7%
06. Pendal Group Limited	2,801,726	1.6%
07. The Vanguard Group, Inc.	2,638,027	1.5%
08. Vanguard Investments Australia Ltd.	2,576,764	1.4%
09. Accident Compensation Corporation	2,468,565	1.4%
10. Salt Funds Management Limited	2,407,877	1.3%
11. First NZ Capital Custodians Limited	1,580,271	0.9%
12. Norges Bank Invesment Management	1,570,360	0.9%
13. First Sentier Investors Realindex Pty Ltd.	1,202,153	0.7%
14. BlackRock Institutional Trust Company, N.A.	1,130,798	0.6%
15. Paul & Bronwyn Lancaster	1,058,123	0.6%
16. Smartshares Limited	957,743	0.5%
17. Abu Dhabi Investment Authority	915,436	0.5%
18. Therese Roche	900,000	0.5%
19. Guardians of New Zealand Superannuation	807,381	0.5%
20. ANZ New Zealand Investments Limited	806,403	0.4%
Total	147, 085, 301	81.9%

[1] Note this is FIL Limited Group's total holding. FIL Investment Management (Australia) Limited holds 4.2% or 7,491,149 shares, FIL Investment Management (Hong Kong) Limited holds 1.0% or 1,818,323 and FIL Investment Management (Singapore) Ltd. Holds 0.2% or 283,126 shares.

According to notices given under section 280(1)(b) of the Financial Markets Conduct 2013, the following are Synlait's substantial product holders as at 31 July 2020. The number of shares owned is as advised by the shareholder in their last Substantial Security Holder Notice.

Substantial Product Holder	Number of ordinary shares in which relevant interest is held	Percentage of Ordinary Shares owned as at 31 July 2020
Bright Dairy Holding Limited	69,968,944	39.0
The a2 Milk Company Limited	35,574,646	19.8
FIL Group Limited	9,592,598	5.3
Total		64.1%

Set out below are Synlait's 20 largest bondholders as at 31 July 2020:

	Number of bonds held	Percentage of total bonds
01. TEA Custodians Limited Client Property Trust Account	21,400,000	11.89%
02. FNZ Custodians Limited	20,780,000	11.54%
03. Investment Custodial Services Limited	15,297,000	8.50%
04. Custodial Services Limited	13,059,000	7.26%
05. Forsyth Barr Custodians Limited	10,965,000	6.09%
06. Custodial Services Limited	8,269,000	4.59%
07. National Nominees Limited	6,597,000	3.67%
08. Custodial Services Limited	6,417,000	3.57%
09. Citibank Nominees (New Zealand) Limited	4,400,000	2.44%
10. Custodial Services Limited	4,216,000	2.34%
11. Custodial Services Limited	3,702,000	2.06%
12. RGTKMT Investments Limited	3,275,000	1.82%
13. JBWare (Nz) Nominees Limited	2,855,000	1.59%
14. Custodial Services Limited	1,174,000	0.65%
15. FNZ Custodians Limited	1,038,000	0.58%
16. Hugh McCracken Ensor	1,000,000	0.56%
17. Investment Custodial Services Limited	1,000,000	0.56%
18. Francis Horton Tuck	800,000	0.44%
19. Investment Custodial Services Limited	800,000	0.44%
20. FNZ Custodians Limited	718,000	0.40%
Total	127,762,000	70.98%

11. SPREAD OF PRODUCT HOLDERS

The spread of Synlait's ordinary shareholders as at 31 July 2020 is as follows:

Size of holding	Number of investors	Percentage of investors	Total number of shares	Percentage issued
1 – 1,000	2,412	40.98%	840,900	0.47%
1,001 – 5,000	2,480	42.13%	5,399,824	3.01%
5,001 – 10,000	547	9.29%	3,662,484	2.04%
10,001 – 50,000	368	6.25%	6,418,611	3.58%
50,001 – 100,000	29	0.49%	1,936,921	1.08%
100,001 and over	50	0.85%	161,048,168	89.82%
Rounding		0.01%		
Total	5,886	100%	179,306,908	100%

The spread of Synlait's bondholders as at 31 July 2020 is as follows:

Size of holding	Number of holders	Percentage of holders	Total number of bonds	Percentage issued
1 – 1,000	0	0%	0	0%
1,001 – 5,000	54	4.81%	268,000	0.15%
5,001 – 10,000	160	14.26%	1,573,000	0.87%
10,001 – 50,000	671	59.80%	19,392,000	10.77%
50,001 – 100,000	138	12.30%	11,637,000	6.47%
100,001 and over	99	8.82%	147,130,000	81.74%
Rounding		0.01%		
Total	1,122	100%	180,000,000	100%

12. CREDIT RATING

Synlait does not have a credit rating.

13. NZX WAIVERS

Synlait obtained two sets of waivers from the NZX Listing Rules this year, relating to a transaction with The a2 Milk Company Limited and Synlait's governance arrangements.

Waiver related to variation of Nutritional Powders Manufacturing and Supply Agreement

In 2019, a wholly owned subsidiary of Synlait entered into a variation of its existing Nutritional Powders Manufacturing and Supply Agreement with a wholly owned subsidiary of The a2 Milk Company Limited. As the variation may have been worth more than 50% of Synlait's average market capitalisation, and The a2 Milk Company Limited is a related party of Synlait, the NZX Listing Rules require that the variation is approved by shareholders and that an appraisal report on the variation is obtained. On 15 November 2019, Synlait was granted waivers from the relevant NZX Listing Rules so that shareholder approval to, and the appraisal report on, the entry into that variation were not required. To the extent that the waiver applied to the requirement to get shareholder approval of a related party transaction, the waiver was conditional on the Directors of Synlait certifying that:

- the terms of the variation were negotiated and entered into on an arm's length commercial basis;
- Synlait was not unduly influenced by The a2 Milk Company Limited to enter into the variation; and
- entry into the variation was in the best interests of all of Synlait's shareholders.

The Directors of Synlait provided a certificate to this effect to NZX.

Waiver relating to Governance Arrangements

On 27 November 2019, Synlait was granted new governance waivers, designed to be consistent with the new NZX Listing Rules introduced by NZX on 1 January 2019. These allow our Constitution and Board composition to reflect our non-standard governance arrangements, as described below, and replace our previous governance waivers granted on 24 June 2013 and amended on 30 October 2018.

Synlait listed on the NZX on the basis that Bright Dairy and Food Co Limited would be able to continue to consolidate Synlait into its group financial statements (that are prepared under China GAAP). At the time, Bright Dairy agreed with Synlait that for so long as Bright Dairy continued to hold between the Initial Percentage (being 39.119%) and 50% (inclusive) of the shares in Synlait in each case calculated in accordance with clause 22.5 of the Constitution (so as to exclude shares issued under employee share schemes or director remuneration), the following governance arrangements will apply to Synlait:

The Board will comprise eight directors, made up of the following:

- Four directors appointed by Bright Dairy (the **Bright Dairy Directors**):
    - none of whom (i) would be required to retire from rotation under the NZX Listing Rules, or (ii) are subject to removal by ordinary resolution of shareholders;

    - one of whom must be ordinarily resident in New Zealand and be a director of such standing and with such commercial and governance experience in New Zealand as is appropriate for a director of a NZX listed company – the Hon. Ruth Richardson is the current Bright Dairy Director meeting this requirement; and
    - all of whom are required to have appropriate skills and experience to ensure that Synlait has a suitable mix of skills and experience on the Board;
- Three directors who are not appointed by Bright Dairy and who must be Independent Directors; and
- One Managing Director, or, if a Managing Director is not appointed, a Board Appointed Director, who will be appointed by the Board. The current Managing Director or Board Appointed Director, and any Director proposed to fill that role, cannot vote on the appointment or replacement of the Managing Director or Board Appointed Director (as applicable). Consequently, Bright Dairy controls the composition of the majority of the Board as it would have four out of seven votes on this appointment. Synlait does not currently have a Managing Director, but does have a Board Appointed Director, being Dr. John Penno,

(together, these are the **Governance Arrangements**).

A summary of the waivers permitting these Governance Arrangements is set out below:

- The NZX Listing Rules allow Bright Dairy to appoint representatives to the Board so long as the proportion of the Board made up by their representatives is not greater than the proportion of the total shares in Synlait that they own. A waiver was required to permit Bright Dairy to appoint four Directors, or 50% of the Board, as Bright Dairy owns less than 50% of the shares in Synlait.
- The NZX Listing Rules prevent Directors from appointing alternates to act for in their place if they cannot attend Board meetings, unless a majority of their co-Directors agree. A waiver has been granted to permit Synlait's Constitution to:
    - allow a Bright Dairy Director to appoint another Bright Dairy Director to exercise their voting rights at a Board meeting they are unable to attend; and
    - prohibit the non-Bright Dairy Directors from appointing alternate Directors. Synlait considers that it is important that Directors are encouraged to attend all meetings.
- The NZX Listing Rules require that Synlait's constitution permit a Director to vote on a decision in which they are interested, where that matter is one in respect of which Directors are required by the Companies Act 1993 to sign a certificate, or relates to an indemnity contemplated by section 162 of the Companies Act. A waiver has been granted to allow Synlait's Constitution to prohibit the Managing Director (if it has one, which it doesn't currently) from voting or being part of the quorum on matters relating to his/her remuneration under any circumstances.
- The NZX Listing Rules prevent the imposing of conditions on who may be appointed as a Director, except as specifically contemplated by the Rules. A waiver has been granted so that Synlait is permitted to required that persons who may be appointed to the three non-Bright Dairy Director positions must be independent.

These waivers are subject to the conditions that:

- Bright Dairy continues to hold no less than 39.119% of Synlait's shares, calculated in accordance with Synlait's Constitution.
- the Governance Arrangements are contained in Synlait's Constitution and will cease to apply when Bright Dairy ceases to own between 39.119% and 50% (inclusive) of the shares in Synlait, calculated in accordance with Synlait's Constitution.
- Full and accurate disclosure of all material aspects of the Governance Arrangements and Synlait's reliance on these waivers is made in any offer document, and in every annual report while these waivers are being relied on.
- Synlait continues to bear a non-standard designation to notify the market of its unique governance arrangements.
- The quorum for a Board meeting must include two Independent Directors, and Synlait must have three Independent Directors (compared to the two Independent Directors required by the NZX Listing Rules).
- Immediately on Bright Dairy ceasing to hold 39.119% of the shares in Synlait, Synlait complies with the provisions in its Constitution requiring that some of the Bright Dairy Directors must resign to keep the proportion of Bright Dairy Directors on the Board consistent with the proportion of the total shares in Synlait owned by Bright Dairy. Also, all remaining Bright Dairy Directors must retire by rotation at the next annual meeting following the drop in shareholding below that threshold, irrespective of whether they have been the longest in office.

As noted above, on 1 January 2019, NZX updated the NZX Listing Rules. In order to assist with transition to the new NZX Listing Rules, NZX granted the class waiver called "Class waivers and rulings for NZX Main Board and Debt Market Transition", dated 19 November 2018, which had effect until 30 June 2020 (**Class Waiver**). The class waiver allowed Synlait to continue relying on its governance waivers under the old NZX Listing Rules, from its transition date to the new NZX Listing Rules on 8 March 2019, until the governance waivers were updated on 27 November 2019. As required by the class waiver, Synlait sets out below a summary of the governance waivers under the old NZX Listing Rules, as issued on 24 June 2013 and amended on 30 October 2018 (**Original Governance Waiver**).

The Governance Arrangements as described above were also permitted under the Original Governance Waiver, together with the following additional governance arrangements:

- The Board Chair, who must be an Independent Director, will have a casting vote. The Chair of the Audit and Risk Committee must also be an Independent Director.
- No Director will have the right to appoint an alternate Director to act in his or her absence or unavailability, but any Bright Dairy Director may appoint another Bright Dairy Director to exercise his or her voting rights at a meeting.
- A quorum of the Board must include at least two Independent Directors.

(together with the Governance Arrangements, these are the **Original Governance Arrangements**).

The summary of waivers described above in the context of the current Governance Waiver is also applicable to the Original Governance Waiver (given Synlait's reliance on the Class Waiver in respect of the corresponding rule under the old Listing Rules). The Original Governance Waiver also comprised the following additional waivers:

- The then current NZX Listing Rules required one third of Synlait's Directors to retire by rotation at each annual meeting. Waivers were granted so that:
  - the rotation requirement only applied to Independent Directors, and not to Bright Dairy Directors and Managing Director or Board Appointed Director;
  - one out of the three Independent Directors was required to retire each year;
  - at the first annual meeting following the Bright Dairy shareholding falling below 39.119% (calculated as provided by the Constitution, excluding employee and director share issues made pursuant to the NZX Listing Rules), all Bright Dairy Directors would be required to retire by rotation, even though they may not have been longest in office.
- The then current NZX Listing Rules prevented Synlait from imposing restrictions in its constitution on the right of shareholders to transfer shares held in Synlait, or any restrictions upon registration of a properly completed transfer of such shares. A waiver was granted so that Synlait's constitution may contain certain restrictions on the right of shareholders to transfer Synlait shares, as applied under Schedule 2 of Synlait's constitution which was removed on 27 November 2019.

These waivers were subject to the conditions that:

- Bright Dairy held no less than 37% of Synlait's shares at the date Synlait was listed.
- the Original Governance Arrangements were contained in Synlait's Constitution and would cease to apply when Bright Dairy ceases to own between 39.119% and 50% (inclusive) of the shares in Synlait (calculated as provided by the Constitution, excluding employee and director share issues made pursuant to the NZX Listing Rules).
- Full and accurate disclosure of all material aspects of the Governance Arrangements and Synlait's reliance on these waivers is made in the offer document issued at the time of Synlait's listing, and in every annual report while these waivers are being relied on.
- Synlait continues to bear a non-standard designation to notify the market of its unique Governance Arrangements.
- Synlait appoint an additional Independent Director as soon as possible, but in any event within 3 months of listing.
- That for so long as Bright Dairy holds between 39.119% and 50% (inclusive) of the shares in Synlait (calculated as provided by the Constitution, excluding employee and director share issues made pursuant to the NZX Listing Rules), Synlait complies with the following clauses of its Constitution: 25.7, 6-11 (inclusive) and 13 of Part A of Schedule 1.
- Immediately on Bright Dairy ceasing to hold 39.119% of the shares in Synlait, Synlait complies with the provisions in its Constitution requiring that some of the Bright Dairy Directors must resign to keep the proportion of Bright Dairy Directors on the Board consistent with the proportion of the total shares in Synlait owned by Bright Dairy. Also, all remaining Bright Dairy Directors must retire by rotation at the next annual meeting following the drop in shareholding below that threshold, irrespective of whether they have been the longest in office.

Copies of these waivers, and other waivers Synlait has obtained, or relied on before 1 August 2019 can be found in the investor centre of Synlait's website.

14. GENDER COMPOSITION

This table sets out the gender recomposition of Synlait's Directors and Officers (CEO and direct reports to CEO) as at 31 July 2020. The prior year's comparison is in brackets.

Group	Female	Male	Total
Board	2 (2)	6 (6)	8 (8)
Officer	3 (2)	6[1] (9)[2]	9 (11)
Total	**5 (4)**	**12 (15)**	**17 (19)**

[1] Includes one officer employed by a subsidiary but reporting to the CEO

[2] The 2019 figure includes two male General Managers who temporarily reported to the CEO pending the appointment of new Director Operations in December 2019

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